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LYBRAND JOURNAL

The Audit of the Cost System*

By John J. Fox

A substantial amount of accounting literature has been devoted to the development and design of cost accounting systems while little attention has been given to the procedures followed by the certified public accountant in auditing the cost system. The cost system is the focal point of the financial audit of manufacturing concerns and is a mechanism for applying sound accounting principles to the problem of allocating the total cost pool (consisting of opening inventories, material purchases, labor costs and manufacturing expenses) between current and future accounting periods. While consideration must also be given to economic factors such as replacement costs and realizable values, cost is the primary basis for inventory valuation. The audit of manufacturing costs is usually best accomplished through a review of the cost accounting system.

Objectives of the Cost System Review

This discussion is restricted to the investigation of the cost system which is made as an integral part of an audit with the objective of expressing an opinion on the financial statements. It excludes consideration of special studies relating to control over processing of paper work, control over inventories and the development of more useful management data from the cost system which the C.P.A. may be called upon to provide as a service to management.

The auditor should review the cost system with three principal objectives in mind:

1. Ascertaining the propriety of cost allocations between current and future periods (i.e., determining the appropriate amounts for valuation of inventories).

* Reprinted by permission from *The New York Certified Public Accountant*, April, 1960.

2. Ascertaining that the sytem provides appropriate accounting controls over costs incurred and related inventories.

3. Ascertaining that the cost accounting process is handled economically and provides management with effective information for controlling and reducing costs, determining product cost and profitability, etc.

The third objective stated above may be the subject of special management services assignments for the C.P.A. However, the auditor frequently has opportunities for making constructive comments and recommendations to management as a result of his observations during an audit.

Over-all Review of the Cost System

An initial investigation of the nature and type of cost system in use is usually required to provide a basis for developing a detailed program for auditing the cost system. This initial investigation should be sufficiently comprehensive to enable the auditor to plan a program for testing and evaluating the cost system. Some of the techniques that are available to the auditor for this initial over-all review are:

1. Touring the client's plant facilities.
2. Reviewing internal financial statements and analytical cost reports.
3. Reviewing company accounting manuals.
4. Preparing system outlines.

Touring the Client's Plant Facilities

To make an effective analysis of a cost system, the auditor should have a general understanding of the nature of the company's products, its manufacturing facilities and processes and the flow of materials through the plant. This information can usually be best acquired by touring the manufacturing and storage areas of the plant. During the plant tour, the auditor should observe:

1. The nature of the materials received.

2. The flow of the materials from the receiving areas into the storage areas and the documents accompanying such movements.

3. The arrangement of the manufacturing facilities and processes and the flow of the materials through these processes.

In this manner, the auditor becomes familiar with the character of the operation as being one that brings many raw materials into a single end product, or one that separates a single raw material into several end products. He should also note the points at which the processed materials emerge as salable products in the different phases of the production process.

The auditor should also observe how semifinished and finished products are stored, the physical movement of materials shipped to customers and the introduction of semifinished materials into the production process together with the handling of the related paper work.

During the course of the plant tour, the auditor usually meets some of the key manufacturing personnel. Such personnel are usually pleased to explain what they are doing and what their problems are. These contacts provide the auditor with an insight into production problems; he may also become aware of problems relating to excess or obsolete materials and scrap and spoilage. He can inquire about timekeeping procedures, whether work standards are used and how production is scheduled. He should obtain definite impressions of shop housekeeping, the general attitude of shop personnel toward accounting control and an understanding of plant terminology that will enhance his ability to communicate with his client's personnel.

A plant tour in a medium-sized manufacturing establishment may require no more than several hours. It serves to orient the auditor's thinking on the overall assignment. He may, of course, require subsequent visits to the plant as his work progresses. The plant tour may provide an opportunity to obtain an organization chart for manufacturing. In some companies such a chart will be readily available and can be supplied to the auditor without difficulty. In other instances, it may be necessary for the auditor to prepare a rough draft of such an organization chart by drawing upon the knowledge of company personnel. A schematic diagram of the production process is also a helpful tool.

Reviewing Internal Financial Statements and Analytical Cost Reports

The initial procedures in any audit should include an over-all review of financial statements to give the auditor perspective as to the financial position of the company, types of assets and liabilities, results of operations and similar general financial information. In approaching the audit of the cost system, this review of financial statements should be extended to include cost reports. The auditor should request copies of all recurring cost reports as well as examples of special cost studies. The examination of recurring cost reports will disclose the type of information generally available from the existing system. The auditor, of course, should specifically seek information as to the product classifications used in the cost

system, the departmental organization recognized in the accounting records, whether standard costs are used, and whether the standard costs appear to bear a reasonable relationship to recorded costs. He should also be interested in the results of the company's own analytical efforts. Both the regular and the special reports may furnish leads to more complex questions that the auditor might wish to investigate.

Reviewing Company Accounting Manuals

Many companies are equipped with comprehensive manuals covering all phases of the accounting procedures. Where manuals are in existence, the sections relating to cost accounting procedures should provide the auditor with an extensive knowledge of such procedures. In some instances, procedural descriptions will be accompanied by flow charts and other illustrative material. When information is available from this source, it will quickly supply the auditor with ready-made answers that could otherwise be secured only by more extensive field investigations. When such information has been recorded in accounting or procedures manuals, it is unnecessary for the auditor to spend time transcribing this information for his work papers.

Preparing System Outlines

The ultimate objective of the over-all investigation of the company's cost accounting system is to enable the auditor to appraise and understand the cost system and to enable him to test and evaluate it. To the extent that the previously described over-all approaches have failed to complete the auditor's understanding, that deficiency should be remedied by other investigations which may include preparing comprehensive system outlines based upon discussions with supervisory personnel, and an inspection of cost records.

Detailed Testing of the Cost System

The over-all review of the cost system should give the auditor sufficient familiarity with the cost records to enable him to use them inteligently in reviewing the pricing of inventories. It may also provide the auditor with sufficient insight into the application of accounting principles in the cost procedures to enable him to draw some tentative conclusions as to the reliability of the system. At this point, however, the auditor's conclusions are probably

based on insufficient evidence since he has not yet ascertained whether the procedures described to him or outlined in accounting manuals are being followed nor has he ascertained the quality of the underlying clerical work.

Cost accounting procedures in many companies require the processing of a substantial volume of underlying paper work. Material requisitions and labor distributions can be quite voluminous in large plants where the end product is the work of a large group of timekeepers, stores clerks and other personnel. Expense distributions can be complicated. Frequently accounting data are summarized first by individual departments and then resummarized in successive steps until a final distribution is obtained. Service department expenses often require complex allocation procedures.

The immediate objective of the auditor is to devise procedures for testing the cost system effectively with a minimum expenditure of time. The nature of the investigation must be adapted to the particular system in use. The character of the testing may be very different for different types of cost systems. Certain general principles of testing apply, however, in most circumstances. The types of detailed tests which can be applied in most instances are classified as follows:

1. Test of distribution of original charges and credits.
2. Analysis and review of cost and inventory accounts.
3. Review of cost allocation procedures.
4. Consideration of budgetary factors.

Distribution of Original Charges and Credits

Auditors customarily organize a program into a series of functional tests and reviews of account balances. These tests serve to probe deeply into the business organism. Many of the functional tests should be programmed to provide the auditor with authentication of data entering into the cost system. Some of the functional tests that bear upon the cost system work are tests of purchases, payrolls and sales; tests of internal charges, such as work orders and requisitions, are also related to the cost accounting system.

Tests of purchases are undertaken with the primary objective of substantiating procedures for the disbursement of funds. Each disbursement, however, originates an account charge, primarily to inventory or expense accounts. These charges are the original

entries in the cost procedure. Consequently, the auditor must be concerned with establishing not only the authenticity of such charges, but also the consistency and reliability of their classification to appropriate inventory or expense accounts. Such charges should be traced through on a test basis to entries in detailed inventory and expense ledgers.

Payrolls are also examined primarily for substantiation of disbursements. Procedures for recording payroll distribution should be examined and tested to substantiate cost entries originating from payroll charges. The auditor should also investigate the timekeeping procedures as part of this process since eventual account charges can be no more reliable than the original time charges.

The sales examination also has its interrelationship with the cost system investigation since the summarization of product shipments is the basis for relief of inventories and charges to cost of sales. The auditor should review and test the procedures for summarizing quantities of products sold and the cost applied to sales for the resultant determinations of cost of sales and inventory relief entries. Attention should be given to the classification of product shipments and to the treatment of other items such as scrap and byproduct sales.

Although functional tests of sales, purchases and payrolls are made primarily for reasons other than cost system analysis, such tests may also be used to substantiate cost accounting procedures. In addition, tests should be made of charges for materials transferred to production, accounting for scrap and spoiled production, the determination of standard unit costs and the recording of operating variances where standard costs are used.

Analysis of Costs and Inventory Accounts

In his preliminary investigation of the cost system, the auditor frequently develops a schematic diagram of the cost system accounts, indicating the flow of the elemental costs through the system. The auditor should investigate the actual operation of the system by analyzing selected accounts and tracing the entries in these accounts back to source records which have been authenticated by other audit procedures. The analysis of entries in the cost and inventory accounts serves to tie together the various phases of the auditor's work. Account analyses may disclose entries from sources not yet tested which should be investigated. Such entires frequently provide a deeper insight into the account-

ing principles applied and the method of their application and expose unusual or nonrecurring transactions for review.

Review of Cost Allocation Procedures

Manufacturing cost accounting is essentially a procedure for first accumulating costs by type in the centers where they are incurred and then allocating the accumulated costs to individual products. Fixed costs such as rent and depreciation charges on buildings contribute to the value of the products produced but cannot be associated readily with individual products other than through some method of allocation. In some instances, such costs may be allocated to individual products as a burden rate applied on the basis of direct labor. In other instances, more refined studies may be developed under which depreciation, for example, may be allocated to products on the basis of floor space used or power on the basis of metered consumption. The auditor, in any event, should be sufficiently versed in industrial accounting practices to review the reasonableness of the allocation procedures and the consistency with which the procedures are applied.

Production standards for material, labor and overhead are essentially devices for predetermining cost allocations based on normal usage of the various cost components. Such standards frequently provide a more reliable method for measuring costs than so-called "actual" cost methods. The auditor should, of course, have some knowledge of the basis on which such standards were determined. This can be accomplished partially through a review of the underlying specifications and standard procedures and partially through the review and analysis of the resultant variance accounts. The auditor should ascertain whether the standards are maintained on a current basis and revised for current changes in conditions. He should also ascertain whether they are set in a manner designed to measure normal costs and result in charging inefficiency losses to the current accounting period.

Consideration of Budgetary Factors

Manufacturing costs are drastically influenced by volume changes due to the influence of the cost behavior of fixed and variable expenses. While certain expenses will vary directly with volume, other expenses will remain relatively fixed in amount. When volume is high, unit fixed costs are low and, conversely, as volume decreases, unit fixed costs tend to increase. Direct costing

procedures segregate fixed costs so that unit costs consist only of variable direct costs which, in theory, are not subject to fluctuation when volume changes. Year-end balance sheet adjustments may be required to include appropriate amounts of fixed costs in inventory where standards for pricing inventory include only direct costs.

When absorption costing procedures are used, product costs tend to vary conversely with volume changes. When volume is low the accountant should recognize the possible existence of idle plant costs which should be treated as period charges and should not be allocated to inventory values. This is frequently accomplished by determining normal volume and establishing standard overhead rates on cost levels anticipated for normal volume. The auditor should review the basis for determining normal volume and establishing the standard overhead rates.

Program for Audit of a Cost System

A sample audit program for the audit of a job cost system is described in the following paragraphs. The audit functions relating to the physical tests of inventory quantities and inventory pricing have been excluded from this program because the discussion is limited to the basic problems of reviewing the cost system. While certain portions of the program will relate equally well to both a job order and process cost system, certain revisions would be appropriate in adapting such a program to a process cost system.

Tour the plant with supervisory plant personnel in order to become generally familiar with the production processes, the flow of production materials in the manufacturing process and the organization of the plant.

Ascertain the general nature of the cost accounting system and the procedures in effect by inquiring of the cost accounting supervisor and reviewing the company's internal financial statements and cost reports.

Select an interim accounting period and review the entries recorded in the inventory and cost of sales accounts. Trace amounts to source of entry and test and review underlying details for other than purchases and payroll entries which were tested in other phases of the audit.

Trace charges on a test basis to work in process for actual costs of material and labor from source data to the job order cost cards (refer to step above).

Test the pricing of charges to work in process for material and labor at standard by reference to standard cost records.

Review the procedures for closing job orders with responsible employees. Select a representative sample of job orders closed during the period; review the relat d job order cost cards, test the computation of the variances and trace to the journal entry.

Review the methods of accounting for scrapped production and scrap materials resulting from the production processes.

Compare the total of sales summarized for costing purposes with recorded sales for the test period to determine that all sales are included in the costing.

Test costing of sales for items selected from costing tabulations by reference to standard cost records.

Review the methods and procedures for establishing standard costs and ascertain that standards have been revised to reflect current conditions.

Test selected items to determine that standards are representative of cost by comparing the standard unit costs with actual costs recorded on the cost cards for completed job orders.

Ascertain the nature of production cost variances and their relationship to the total cost of production to form an opinion of the acceptability of the standard cost for inventory pricing purposes.

Review the computation of the standard burden rates to determine that such rates result in charging period costs to current operations and do not defer such charges to future periods.

Review inventory and cost of sales accounts for other periods in the year and investigate any entries of significant amount or from unusual sources.

Constructive Results from an Audit of the Cost System

As a result of his audit of the cost system, the auditor is frequently in a position to make constructive suggestions to his client. Such suggestions can be important in enabling the company to operate more profitably. Large companies as well as small can always profit from independent appraisals of their cost accounting procedures.

The author recalls one instance in which a manufacturing concern produced two different products in two different departments of the same plant. The manufacturing process in one department was highly mechanized, requiring a substantial investment in the equipment and utilizing very small amounts of direct labor. The second department required little equipment investment and substantial amounts of direct labor. The product cost accounting procedures of this company consisted of accumulating the cost of material and direct labor for each product and allocating overhead accumulated on a plant-wide basis by means of an overhead rate applied to direct labor. The result of this procedure was, of course, that the depreciation costs and overhead of the first department were substantially charged to the products produced in the second department. It is not surprising that the products produced in the second department consistently showed a loss while unfortunately management was directing its attention

toward promoting the supposedly very profitable product of the first department.

It should be noted that in instances where products pass through all departments of the plant, a plant-wide overhead rate usually produces an equitable result for product costing purposes. However, departmentalization may be required for purposes of overhead control.

Effective cost accounting procedures are an important factor in physical control over materials. When inventory controls are not effective they frequently contribute to spoilage, pilferage and other losses which may be far more costly than the losses that are likely to result from careless handling of other assets such as cash.

In one cost system audit, inquiries concerning the handling of scrap disclosed that the company was suffering substantial losses on the disposition of scrap because of its failure to properly segregate and classify different types of scrap. Failure to provide effective internal controls over the disposition of scrap has undoubtedly been responsible for many inventory losses.

Auditors frequently encounter manufacturing cost systems which provide the required tools for product cost determinations but do not provide management with tools for controlling and reducing material, labor and overhead costs. Cost accounts should be organized in a manner that facilitates placing the responsibility for costs incurred upon appropriate individuals in management. The accounts should provide a mechanism either through standards or other similar methods of comparison for determining the reasonableness of costs incurred. When such controls are not built into the accounts, the auditor should advise his client of the deficiencies.

In many instances, substantial sums are expended in the clerical processing work related to manufacturing operations. The auditor should always be alert to indications of inefficiencies in the clerical processing methods. Many companies have achieved substantial savings not only in the cost of clerical processing but in the manufacturing operations themselves by improvement in forms design and procedures for handling of clerical work. Tabulating and other processing systems have been adopted to coordinate production and inventory control activities. The auditor should be sufficiently familiar with these techniques to enable him to recognize opportunities for recommending improvements in the handling of such activities in the client organization.

In audits of manufacturing organizations, the audit of a cost system provides the auditor with one of the best areas of rendering valuable service to his clients. In order to utilize this opportunity, the auditor should be soundly grounded in cost accounting procedures and thoroughly familiar with his client's manufacturing processes and products. He must be constantly alert for opportunities to apply his professional knowledge in a manner most beneficial to his client.

Moral Responsibility in Tax Practice*

A Former IRS Official's View

By Clifford W. Stowe (Washington Office)

It has been pointed out that the professional tax practitioner has multiple responsibilities; to his client, his government, his profession, and himself; and that the several interests which he serves at times are in sharp conflict with each other. As Albert H. Cohen so well said, "Conflicts between them can and do arise that may require the wisdom of a Solomon and the fortitude of a David."[1] What is true of the practitioner is also true to a degree with respect to the government employee and the taxpayer. Hence, with conflicting interests and the everchanging facts and circumstances with which we are confronted in tax practice and administration it would be unwise, to say the least, to attempt to be dogmatic or categorical as to any set of rules of conduct.

Among the many fine characteristics of the American people are their deep-seated sense of fair play and their loyalty to their government. These must be preserved. Most immediate is the necessity for preservation of their belief in the basic justice of the tax laws and their administration.

The results we have seen in other countries of a combination of unjust tax laws and weak, incompetent or venal administration should be enough to alert all of us to the need for our active interest and effort in preserving our self-assessment tax system and the highest degree of voluntary compliance.

Preservation of the self-assessment system does not, however, necessarily mean preservation of the status quo or that we are deprived of our right as free born American citizens to make constructive criticisms. To the contrary, it means to me that we have a duty, through active and aggressive interest and criticism directed in proper channels, to constantly work for improvement of the status quo and to so set our standards of conduct that we

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* This paper appeared originally as one of a series of three on the general topic of moral responsibility in tax practice. Minor changes have been made to remove references to the companion articles. Reprinted by permission from *The Journal of Accountancy*, April, 1959.

[1] Cohen, Albert H., "Professional Conduct in Taxes," JofA, Jan 56, p. 34.

provide an outstanding example of leadership as public-spirited citizens as well as members of professions which deserve and receive the respect and confidence of the people of this country.

To accomplish these high purposes what are the things we should do and what are the things we may not do? I will try to state briefly my views as to the responsibility of the taxpayer, and then discuss my concepts of the responsibilities of the Internal Revenue Service.

Judge Learned Hand, in one of his many brilliant opinions, said "Over and over again courts have said that there is nothing sinister in so arranging one's affairs as to keep taxes as low as possible. Everybody does so, rich and poor; and all do right, for nobody owes any public duty to pay more than the law demands; taxes are enforced exactions, not voluntary contributions. To demand more in the name of morals is mere cant."

On the other hand the taxpayer has a responsibility for honesty, truthfulness and obedience. If he believes that the law is unjust, or its administration is unfair and improper, his recourse should be through petition to the administrator, the courts, his duly elected representatives, or through exercise of his franchise.

In 1875 Noah H. Swayne, Justice of the U.S. Supreme Court, stated that citizens are bound to exhibit truth, frankness and integrity in their dealings with their government, and the government officer in the discharge of his duties should be animated solely by considerations of right, justice and the public good.[2]

Responsibilities of the IRS

More specifically, what are the responsibilities of the Internal Revenue Service? Basically it seems to me that the Service has a responsibility to provide an honest, competent, consistent, fair and even-handed administration of the taxing statutes giving due regard, in its interpretation and administration to the will and intent of the legislature, when that will and intent may be ascertained.

How can the Internal Revenue Service implement and discharge its responsibilities and what is it doing in this regard?

First, the most competent available personnel must be employed, and second, all proper steps taken to insure that the highest possible standards of integrity are established and maintained.

[2] *Trist* v. *Child*, 88 U.S. 441.

The next responsibility is that the employees be trained to properly discharge their duties. The training should extend not only to assure technical competence but also a proper understanding of responsibility to the taxpaying public.

Next, the Service must do everything reasonably within its power to assure the taxpayer of the earliest possible finality of determination of his tax liability consistent with sound and just administrative practices. Concurrently, there must be a never-ending search for simpler, more efficient, and more economical methods of operation.

Next, adequate administrative appeals facilities must be available to all taxpayers. The taxpayer must not only know of the availability of the opportunity for appeal without disproportionate cost, but also he must be convinced that his appeal will be heard by a disinterested and impartial person who will give judicial consideration to his case and be as interested in the securing or preserving of the taxpayer's rights as he will be in sustaining the initial position of the Service.

A new system of handling appeals was established in the District Directors' offices following the 1952 reorganization of the Service. Its primary objectives were informality and quick resolution of the simpler disputes. A minor organizational change was made about two years ago which undoubtedly has alleviated some of the conditions which had previously been criticized. However, I still question whether the quest for informality and speed has not resulted in some loss of judicial consideration.

Insofar as the Appellate Division is concerned a very substantial improvement has been made in the last four years in expediting the disposition of cases referred to it for consideration. In the aggregate, about 90 per cent of the nondocketed cases are disposed of in six months or less from the time they are received by the Appellate Division.

Rules of Conduct of the IRS

From the standpoint of attitude toward the rights of taxpayers you may be interested in one of the rules of conduct laid down for the guidance of Appellate Division conferees. It is this: "The Appellate Division conferee shall bear in mind that an exaction by the United States Government, which is not based on law, statutory or otherwise, is a taking of property without due process of law, in violation of the Fifth Amendment to the United

States Constitution. The conferee, in his conclusions of fact or application of the law, shall hew to the law and the recognized standards of legal construction. It shall be the duty of the conferee to determine the correct amount of the tax, with strict impartiality as between the taxpayer and the Government, and without favoritism or discrimination as between taxpayers." So long as that rule is adhered to it seems to me that no one can be heard to justifiably complain.

In this same connection I would like to quote an admonition from a circuit court of appeals decision which taxpayers, practitioners and Service personnel alike should bear in mind. It is this: "And the plain, obvious, and rational meaning of a statute is always to be preferred to any curious, narrow, hidden sense that nothing but the exigency of a hard case and the ingenuity and study of an acute and powerful intellect would discover."

Finally, any rulings of the Service which have general interest or application should be publicized. The distrust and suspicion which result from knowledge that so-called "private" or "secret" rulings are issued can only result in undermining public confidence in the administration of the tax laws. In the past this situation was blown up all out of proportion to its real significance and the true conditions. However, as a result of the recommendations of a Congressional Committee, the Service publishes a vastly greater number of its rulings—in fact so many that I seriously doubt the capacity of the average human mind to assimilate them or even to classify them in terms of relative importance.

There is an additional point in this category I would like to touch on. It is with respect to discriminatory legislation. The Internal Revenue Service cannot directly or alone do anything effective in this area and, therefore, if anything is to be done it must be accomplished through the representations of the professions and an aroused public opinion. If public respect for the taxing statutes is to be maintained at a level which will assure continued obedience to and compliance with those statutes something must be done to reverse the trend toward discriminatory class, group, or individual privilege through preferential treatment.

Now, I would like to suggest a few things which practitioners can do to assist the Internal Revenue Service in the discharge of its responsibilities.

The first is in creating a better understanding on the part of clients of what their rights and responsibilities are. The laying

on of the hands of the tax collector is an unpleasant enough experience for all concerned even if everyone respects the rights of others and fully recognizes the others' duties and responsibilities.

Next, I am sure that it is quite unnecessary to say that, insofar as the practitioner is concerned, one of his valuable assets is the respect and confidence of Service personnel with whom he must deal. Once that respect and confidence has been secured, the Service personnel, relying on the integrity of the practitioner, can and will do much to ease his path and that of his client. However, the reliance which the Service representative places on the integrity of the practitioner imposes a duty on the latter to make certain of the accuracy of the oral and written representations he makes in pleading his client's case unless he makes it clear that he assumes no responsibility for their accuracy or completeness.

Occasionally, the problem arises as to how far the practitioner should or may go in assisting the Revenue Service to make its determination of tax liability. This opens up the Pandora's box of problems which make the question of moral responsibilities so vexatious.

Duties of the Practitioner

There are those who hold the view that a practitioner has a responsibility for protection of the revenue in the same sense as that term is attributed to the Revenue Service. Also, there are those who contend that a practitioner should not prepare and file a return unless he is ready to vouch both for its accuracy and its completeness in every respect. In other words, the practitioner should know everything there is to know about the financial affairs of those for whom he prepares tax returns; divulge all the information to the Revenue Service; and, inferentially, resolve all doubtful questions in favor of the government.

However desirable such a Utopian situation may be from the standpoint of the tax administrator, it hardly squares with the facts of life and the rules of their codes of ethics by which the lawyer and the accountant are bound. Furthermore, the rules of the Treasury Department do not require it.

While this is an area in which one most certainly may not be dogmatic, there are authoritative writings which shed light on the problem and furnish guidance as to our responsibilities.

In his excellent book, *Professional Ethics of Certified Public Accountants*, John L. Carey says, "It is generally agreed that the certified public accountant in tax practice as in other fields of practice has a primary responsibility to his client. This need not conflict with his responsibility to the government and the general public. One duty to the client is to help him keep his tax to the minimum legally due—that is, to avoid unnecessary overpayment. He also owes the client a duty, however, to try to keep him out of trouble—to advise him to avoid underpayments of tax that may lead to interest or penalties, and particularly to dissuade him from concealments which might result in charges of fraud." (p. 114.)

"Although there seems to be no clearly defined responsibility on the tax practitioner to satisfy himself that the information presented in a return is complete and accurate, the certified public accountant has an inescapable ethical responsibility to exercise prudence in evaluating the information in the return. He should not close his eyes to obvious inaccuracies, nor readily accept information that his own knowledge might suggest to be in conflict with the facts." (p. 118.)

With respect to the question of what position the practitioner should take in the preparation of a return or its subsequent defense before the Revenue Service, where there is an honest basis for difference of opinion as to what the applicable law is, or how it should be interpreted and applied, or even the interpretation of the relevant and material facts, I have found no specific, authoritative statement. However, I believe a fair, general answer can be derived from what has already been cited.

First, I will again refer to Judge Hand's statement that "nobody owes any public duty to pay more than the law demands . . . To demand more in the name of morals is mere cant." Next, I refer to Mr. Carey's statements that the certified public accountant has a primary responsibility to his client, with, however, an inescapable ethical responsibility to exercise prudence in evaluating the information in the return. However, I do not understand that the C.P.A.'s responsibility to a client extends to complicity in misrepresentation, fraud, or any act which would do violence to his own conscience. Finally, I refer to the Treasury Department requirements that each enrolled agent shall be of good character and good reputation, conducting his practice in an ethical and professional manner, observing the ethical standards of the accounting profession.

Conclusion

Bearing all these factors in mind, it seems to me that, where there is an honest basis for varying interpretations of the relevant and material facts or the application of the law to the facts, the practitioner not only is at liberty to urge the interpretation or application which is most favorable to his client, but that is his duty.

So, to sum up, it seems that we may say that the tax practitioner has a professional responsibility to be as accurate in the preparation of a return as the scope of his engagement and his experience and judgment permit; that he should be frank and honest in all his dealings with the government; and that it is his duty to his client to prepare the return in such a manner as to make certain that the taxpayer's liability is no more, and no less than is legally due.

EDP and the Disenchanted*

Felix Kaufman (*Director, North-East Region, Management Services*)

Because there was so much fanfare when people first began to consider electronic data processing, it was natural that a tool with such radical possibilities would be watched with great interest. Electronic data processing has been evaluated through rumor and gossip, and in management literature almost from the moment the first user pushed the start button. Over a period of two to three years, observations, gossip, and surveys have blended with prejudice and hastily-drawn conclusions to form a general impression of the relative success and failure of EDP. One can hardly escape observing a certain note of disappointment in the evaluations he hears and reads.

I have been most interested in this disenchantment and have continuously compared the generally emerging picture with my own image of EDP. Much of the disenchantment—though not all—I believe stems from distortions caused by irresponsible observation and lack of insight into the general and specific problems of planning and implementation.

Accordingly, I shall attempt to put some of the successes and failures of EDP into a more reasonable perspective. I do this on the basis of my own experience, which includes seeing new EDP situations every week, intermittent but frequent contact with a variety of operating installations, continuous contact with all of the principal manufacturers and other observers, and on a never ending examination of a constantly increasing volume of literature.

How can success or failure be measured? In the electronic data processing business, there are some generally accepted reasons for using a computer and these, of course, are the obvious yardsticks of success or failure. To enumerate:

An important motivation for changing systems is the expectation that clerical costs will be reduced.

The new system should provide better data, either by its ability to manipulate information previously available, or because it can provide useful facts not formerly available.

The new system provides additional benefits by improving the timeliness of data.

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Given these as criteria, how does one go about measuring the effectiveness of systems? Obviously, the best way to get the feel of what's going on is to conduct a survey based upon a careful evaluation of what many users have accomplished.

This would pose many difficulties, not the least of which would be a definition of some standard of efficiency to provide a common starting point and the selection of a valid sample. But of more immediate concern in trying to assess the effectiveness of EDP is the fact that, to my knowledge, such a study has not been undertaken.

Accordingly, I must caution readers that what I have to say and what others have said and written is an assessment of the *mood* of the electronic data processing field. It has been arrived at by formal and informal discussion with users, manufacturers, consultants and others, each of whom has his special point of view, and must lack, to a greater or lesser extent, complete objectivity even concerning his own relatively narrow view of the total scene.

The Mood of the Literature

An important element in the mood of the field—and in my impression of that mood—is of course the literature in the field.

"Assessment" articles began to appear during the Autumn of 1958, starting with an article in the *Harvard Business Review*.[1] Its title, "Never Overestimate the Power of a Computer," foreshadowed what we were about to hear from others taking the electronic data processing pulse. Shortly thereafter, a set of statistics collected by a consultant[2] was widely publicized and it has on at least two occasions during 1958, been quoted by popular publications. These statistics merit some analysis and I will do this later.

About the same time, *Fortune*[3] had a piece dealing with management's indifference in dealing with the entire body of costs not entering into the "cost of goods sold," of which office costs were emphasized as a major segment. It is worth noting the major points made by this analysis:

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[1] Lewis, R. F., "Never Overestimate the Power of a Computer," *Harvard Business Review* (September–October, 1957).

[2] John Diebold, Address to New York City Control of the Controllers Institute of America (March 13, 1958).

[3] Stryker, Perrin, "What Management Doesn't Know Can Hurt It," *Fortune* (November, 1957).

1. It cited the traditional indifference of top management to the office and distribution cost areas.

2. It doubted that there are many cases where more information is needed. This was in connection with the claims made for electronic data processing's ability to produce more information.

3. It quoted a consultant who seemed to imply that there ought to be an important lesson in his own experience in "never recommending a computer."

4. It suspected the direction given electronic data processing programs by controllers, as well as their efforts in controlling costs in their own backyard.

5. It cited what has now become an old saw (do a study for electronic data processing purposes and you'll discover major benefits without going to a computer) as evidence of the need for attention to basic improvements without mechanization.

In general, this article was not favorable to the computer cause.

More recently, we have had a survey article in *Business Week*,[4] which seems to me to be the best assessment to date. It acknowledged many "false starts and mistakes," attributing them in the main to management errors stemming from the difficulties in spawning and directing a project which has unusual internal implications, places stress on established organizational relationships, and wants skills not provided by the previous experience of people assigned to the task. This article concluded on a very hopeful note.

Most recently, the "how-are-we-doing" type of note appeared in *Time*.[5] Bad management was cited again and the accountants' role questioned. Equipment came off relatively unscathed.

This is by no means the entire story. In general, however, the points made in other articles have been about the same and, as often as not, have reflected corridor conversation at conventions.

What are the main points developed by this collective assessment? I would say they are as follows:

Most failures are due to bad planning. The evaluations of these failures, however, have not explored in depth the reasons for bad planning. None, to my knowledge, has explored bad planning as a likely prelude to getting into electronic data processing.

The equipment by and large has been satisfactory, although there are some expressions of dissatisfaction encountered about failure to provide specific abilities.

The manufacturers have oversold the product by exaggerating computer skills and by understating or ignoring costs.

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[4] June 21, 1958.

[5] January 26, 1959.

This is the background against which I would like to consider the question of failure and accomplishment. In general, the mood is primarily one of disillusionment because early expectations were not fulfilled, but this is not necessarily accompanied by a sense of disappointment concerning the future.

Extent of Experience

Before proceeding to a more extensive consideration of the question, I would like to consider the extent of the evidence available for judging progress. This will at the same time serve to comment about the validity of statistics thus far employed to evaluate success or failure. As of the beginning of broad assessments of electronic data processing progress late in 1957 and early in 1958, the picture of use was about as follows:[6]

Type of Installation	*Numbers in Use*
IBM 702	11
IBM 705	73
Univac I	36
IBM 650	750
Datatron 205	81

The important qualifications to this use picture are about as follows: (1) Of the group of machines with the full scope of electronic data processing capacity—large internal memory and extensive magnetic tape facilities—the IBM 705 was predominant. Since the first delivery of that machine was made early in 1956, the average 705 installation was about 18 months old on January 1, 1959. This is hardly long enough to put an integrated program on the air. (2) Of the group of major machines, about 120 in total, a substantial number were in use by government. In general, these systems are not subject to the same tests of effectiveness as commercial systems and should not be included without extensive qualification in an over-all evaluation. (3) Of the group which is largest numerically, the smaller magnetic drum machine, the IBM 650 is dominant. Most of these machines, however, were card input—card output devices, since 650 systems using magnetic tape were not delivered until 1957.

[6] In late 1958, the picture was somewhat as follows:

Type of Installation	*Numbers in Use*
IBM 702	11
IBM 705	95
Univac I	60
IBM 650	800
Datatron 205	100

The conclusions one can draw from this picture are as follows:

There were less than 100 full fledged (large scale) commercial systems in early 1958. They had an average age of about one year.

The smaller machines, being predominantly card dominated, were not of the type to make a real mark on the over-all systems of which they were a part.

In my opinion, the statistical evidence of a year and a half ago was slim. Moreover, the oft-quoted survey I have mentioned earlier based its conclusions on 300 responses. If these tended to represent an evenly distributed sample of the installations then in operation, the influence of major systems was very slight indeed. I conclude that our surveys to date are based upon evidence collected too early in the game.

However, although one may accept this qualification of the quantitative evidence, I must still deal with the general feeling that we are off to a slow start and that this is not completely exonerated by the infancy of the field. Therefore, the goal of this paper now is to consider the why and wherefore of disillusionment, given the absence of a body of conclusive evidence to repudiate that mood.

Right to Flounder

I am surprised to find that all evaluations imply a higher order of competence for managers in general than we really ought to expect. I do not see that we have a good precedent for judging progress according to what progress would be if everyone knew what he was doing. May I call your attention to a point of view I describe by the term Coefficient of Institutional Friction. According to this, no organization ought to be evaluated according to that ideal of efficiency which systems men try to design into a procedure and managers feel they are always striving to achieve in practice. All organizations I know of operate around some level of inefficiency. The norm is forever a condition capable of much improvement. Poor organizations have more than *normal inefficiency*; good ones have less. I assume both types have acquired computers and I see no reason why the organizations with a tradition for doing things the hard way should change their stripes for this type of venture.

Accordingly, I come to the conclusion that some among the users are not capable of an efficient transition even though they may eventually produce what for them is a better system. This is hardly a weakness of electronic data processing—neither the

equipment nor the concept. It is fulfillment of the normal range of expectations when the full range of talent—and lack thereof—tackles a major project.

Electronic Data Processing as a Catalyst

A hazard in judging an electronic data processing program on its face is associated with the foregoing, and also associated with the now famous proposition that a good survey can do so much without using a computer. This proposition certainly seems sound. However, as systems men will generally testify, we have all had experience with many situations where obvious improvements are long overdue, but cannot be achieved because of internal differences, organizational barriers, and other obstacles. In fact, in many cases we would just like permission—which we cannot get—to investigate some of these areas.

There are some situations—and I know of them—where electronic data processing has been undertaken by management knowing that it was the only effective way to eliminate archaic practices and modernize operations, even though careful analysis would reveal that other methods, perhaps less expensive, would do the job. The other methods lack impact and run the ever present risk of being corrupted after the existing organization gets its chance to mold the new system into its own image. In these cases, electronic data processing is being employed as a catalyst to facilitate change that will not otherwise occur. I think this is more often the case than most of us are willing to concede.

It is also worth mentioning that one of the most maligned early systems—one that has influenced the mood of the literature—was installed as a result of management's feeling that it was the best way to produce desirable organizational change. However, outsiders viewing its sluggishness in producing clerical cost savings and other obvious benefits, concluded that its sponsors just didn't know what they were doing.

Organizational Problems

The same kinds of problems that prompt some managements to install electronic data processing for dramatic effect prompt others to proceed in the opposite direction. Perhaps the most common complaint about electronic data processing systems design is its tendency to superimpose itself on existing methods of reporting and cumbersome manual methods. In this frame-

work, it replaces some form of mechanization to produce a more elegant but not necessarily cheaper system. This approach is the favorite whipping boy for the critics. I think I can say a kind word even for those who have taken this tack—that is, if they knew what they were about when they did it.

What's right about this approach? I am convinced that all our talk about the necessity for breaking down departmental barriers treats too lightly the problems of the man who has to do the breaking. It's not an easy task and our trailblazer may know what he's up to when he uses the "infiltration" method—which means, get the system for modest, undramatic changes and then grow into other things. Obviously in the early period of such use, nothing sensational will happen to distinguish the system and it probably will be criticized.

Since this is the tack the unimaginative will also take, it is admittedly difficult to distinguish the bungler from the cunning fellow who proceeds this way deliberately.

I think criticisms of the accountants' role flow to some extent out of the delicacy of these organizational problems. In my experience the accountant is frequently aware of the opportunities lying outside of his own domain, but must give very careful thought to his *modus operandi* when he appears to be intruding into someone else's bailiwick. His life is further complicated by the integrating possibilities inherent in electronic data processing, since we cannot dismiss the controller's problem by telling him to shift electronic data processing responsibility to other departments. More often than not, the well-designed system should embrace his activity and the "outside" one and the latter may flow logically out of the former.

I must also add that many prospective users have created steering committees which appear to include the kind of non-accounting point of view the controller's critics say is needed. Notwithstanding the inherent usefulness of this kind of representation, I would say, without hesitation, that I have not encountered the enlightened attitude among production men and engineers that some imply we should find. If anything, they have had less opportunity than the controller to become acquainted with electronic data processing possibilities and to provide the impetus for a new program.

Role of Equipment

In continuing to cite what I could broadly call the extenuating circumstances behind false starts in electronic data processing,

some consideration needs to be given to the role of equipment. Two points are important.

1. The experience of a few pioneer users who began with systems which we now recognize to have been somewhat limited has been grossly exaggerated by the literature dealing with this topic. The problem was compounded by the willingness of these early users to publicize their programs before results were available. Hindsight also tells us that these early users had serious adaptation problems to solve, which they did not recognize and about which, in a sense, they had a right to do some muddling. Reports about these systems have not put them in the proper perspective, considering these problems of equipment and planning.

2. We have been and still are dominated in numbers of systems by machines which take cards and make cards. These machines are not to be belittled. We have, however, tended to overlook their limitations. To begin, they are only important elements in a punch card system. Therefore, they must be utilized in a daring way if they are to seriously alter the existing procedures. Since this is not likely to happen, the justification for these machines rests mainly on the ability to employ them at a lower cost on a given volume of work now being performed by other machines. It is easy to show that these computers can experience considerable difficulty in getting the cost per unit of work down to or below the devices they displace.

The Real Indictment

Lest anyone conclude that the purpose of this article is simply to whitewash various failures, I shall now turn to criticisms which I share with others. Notwithstanding all of the reasons I have given to explain why management has some right to bungle in this field, there are many examples of atrocious planning in this business. These cases, mixed indiscriminately with the ones that have good excuses, account for whatever degree of disillusionment now exists.

Why the atrocious planning? This is no easy question—and it certainly isn't merely rhetorical, for I have always found the situation difficult to analyze and explain. This makes it difficult to provide you with a satisfactory explanation, but I will try.

My intuitive feeling is that management has approached this problem without the sense of humility it requires. Somehow or other, despite a flood of articles and speeches on traps and pitfalls,

management at large has assumed that it had the experience, presumably from previous systems work, to go into EDP. Accordingly, in case after case, the work has been delegated almost altogether to personnel not properly equipped by training or background to do the job without appropriate direction. Of course, once the job is delegated to weak hands, management is in for trouble. Shortly, it will receive a report of findings which it personally has no competence to evaluate. These are the standard preliminaries to a bad system.

I must broaden the indictment in one respect and take sides with the most derogatory literature in this connection. Many installations are failing to produce predicted savings. This indicts the systems man on two grounds. First, he should have enough experience with "savings" to hedge his bets carefully—nothing is as elusive as the clerical saving attributed to new methods. (Then, why isn't he more careful?) Secondly, he does a bad job in the area of cost analysis. He consistently ignores or understates preparation costs, fails to attempt a forecast of future volume, ignores the peripheral system surrounding the machine, understates the cost of permanent staff, and fails to time with sufficient care to evaluate the overtime requirement. Why? I attribute this both to poor training and failure to realize the importance of the cost analysis.

Management has also overrated the systems role of the manufacturer. On the smaller scale involvements with punch card accounting and bookkeeping machines, he grew accustomed to assistance from manufacturers in basic design. The enormous demands now being made upon manufacturers for service make it very difficult for them to provide the depth required for this kind of systems planning. Moreover, what the manufacturer provides must necessarily be planning oriented to a particular machine, but the right planning should be indifferent to specific equipment up to a point at least. In short, the manufacturer should emphasize his ability to discern areas where his equipment might be used and to prescribe the appropriate use for his equipment, given a broad blueprint.

Conclusions

In summary, this article has attempted to assess progress, or lack thereof, in EDP by paying more attention to the inherent nature of the obstacles and to the complications arising from

them. As matters stand now, I believe the following points describe our present situation:

1. Evaluations of electronic data processing progress to date are not scientific. They are primarily intuitive and represent a mood rather than a measurement.

2. Such disillusionment as currently exists is in some part due to standards of attainment which are too high. We have behaved like perfectionists in our evaluations, without proper regard for the substantial difficulties to be overcome in programs of this kind.

3. Many electronic data processing ventures have been or are unsatisfactory to a greater or lesser extent. This seems to be due to a propensity to mismanage this type of project, probably resulting from underestimating the skills required or from overestimating the value of other types of experience.

4. Nothing in experience to date points to any inherent weakness in electronic data processing. With costs falling and experience increasing, the future is definitely favorable for the role of the computer.

Developing Professional Accountants*

By Raymond G. Ankers (*National Personnel Manager*)

The development of professional accountants is perhaps one of the most vital problems facing our profession today. It is a problem which has a direct bearing on the economics of every accounting practice, and this is true even for those who are not at the present time conducting a practice with the aid of a professional staff.

The future of our profession depends upon the caliber of the people who are in it and upon the people who are entering it. Because of its rapid growth and the expansion of its services, the profession requires a steady and substantial influx of capable young people. Furthermore, the climate in public accounting should be such that good students are attracted to our profession and that good men presently in the profession are encouraged to remain in it rather than using the experience they receive in public accounting as a stepping stone to positions in other fields.

There are certain aspects of developing professional accountants that can be handled best by our professional organizations and there are others that can be dealt with most effectively by practitioners. First, let us review briefly some of the matters which come within the province of our professional organizations and later consider the practitioner's part in this effort.

Here are some of the matters in which our professional organizations take leadership: (1) preparing and directing programs aimed at interesting more capable people to choose public accounting as a career, (2) maintaining adequate standards of education and experience for admission into the profession, (3) sponsoring and directing continuing education programs for those in the profession.

Our professional organizations have been acutely aware of their responsibilities in these areas. They have realized for a long time that we are not getting our share of the better college students. The reason we are not doing so is probably quite obvious. The majority of the better high school students seem to be guided towards careers in medicine, law, or engineering. Of those who

* Reprinted with permission from *The New York Certified Public Accountant*, August, 1959.

enter business schools the glamour of advertising, marketing and management seems to prevail over accounting. Our problem here seems to stem from the fact that even now a substantial portion of the public has little conception of what a career in public accounting would be like or of the opportunities it presents.

In order to alleviate this problem the American Institute of Certified Public Accountants initiated several projects during the past fifteen years directed to college-age and pre-college-age students to encourage them to consider public accounting as a career, pointing out the breadth and depth of our work, its social and economic implications, the challenge it presents, and its satisfactions.

The Testing Program

The Institute's first major project was the development of a testing program to aid college students in determining their fitness for public accounting. Four tests were devised—an Interest Test, an Orientation or Aptitude Test, and Achievement Tests, Level I and Level II. This testing program has been used by several hundred schools throughout the country and in Canada. The test scores which are based on national norms aid college professors in career guidance, and prospective employers in evaluating graduating seniors. An additional value beyond the basic purpose of the tests was the fact that our need for competent and well educated people was made known to those in nonaccounting circles, as a result of the publicity the program received. Our needs were not even as well understood at the time this testing program was started as it is today.

A few years ago an aptitude test was prepared for use at the high school level in an endeavor to guide qualified students into enrolling in an accounting curriculum. Unfortunately, these tests have not had as wide a distribution as hoped for. Probably the reason for this is that most high schools are committed by custom to giving a series of objective tests, starting at the tenth grade or below, and they are not disposed to devote further time to testing for a particular field of endeavor.

A Broad Recruitment Program

About five years ago the Institute sponsored a broad recruitment program. This program included the production of a career film "Accounting the Language of Business" and a career brochure, "Accounting May Be the Right Field for You." Through

the cooperation of the state societies, the career film has been shown thousands of times in high schools and colleges. It has also had a large number of showings on television with an audience estimated in astronomical figures. Because of the number of times it has been shown the demand for the film lessened during the past year. It is interesting to note that in April, 1958, the Council of the Institute appropriated a sum of $60,000 for the production of a new motion picture to replace the present one. The new career film, "C.P.A.", will be ready for release early in 1960.

Educational Standards

Maintaining adequate educational standards for admission to the profession is a primary function of our professional organizations. Our educational standards will, in large measure, determine the quality of the talent we will have for development, and the extent to which we can develop beginners will correlate closely with the quality of the beginners.

The report of the Commission on Standards of Education and Experience for Certified Public Accountants recommends higher educational standards. The Commission is an independent body composed of leaders in the accounting profession and in the teaching profession. The report was the result of a study which took several years to complete. Among other things, the report suggests that an educational background comparable to that now required by New York State is a minimum standard and recommends that over a period of time the minimum be increased to include at least one year of postgraduate study.

New York has met this minimum standard since January 1, 1938. It was the first state to require a baccalaureate degree as a prerequisite for taking the C.P.A. examination and only a few other states now have as high standards. However, the fact that New York State has previously taken the leadership in increasing educational standards may suggest that our Society should give serious consideration to sponsoring higher standards in the near future.

Continuing Education

Continuing education in its broadest sense includes all technical information and training made available to members of the profession after completion of formal college programs. In that

context, our professional organizations have provided a wealth of training for their members. Some of the items which might be so classified are the professional magazines, the case studies, the research bulletins and the excellent technical sessions provided by our own State Society and other societies.

Although this type of training is good, there seems to be a latent demand for a much more ambitious and comprehensive educational program for all members of the profession than we now have. Last year the Council of the Institute authorized a study to lay the groundwork for a broad continuing education program which will aid experienced practitioners as well as young staff members. In the Council's considerations of this matter it was pointed out that many practicing certified public accountants have had inadequate training in some phases of practice; that very few local accounting firms can provide adequate training programs for beginners; and that the increasing demands for services by C.P.A.s in new fields such as management services, estate planning, and audits of specialized industries, suggest that unless facilities are provided for instruction in these areas, it is quite possible that great opportunities may be missed.

It was also pointed out that studies made by the Institute's staff show that the legal profession, the medical profession, engineering, insurance, banking, credit men and the American Management Association have elaborate programs of adult education for members of their group. These programs offer a variety of choices to their members, including home study courses, one-day institutes, courses requiring one evening a week over a period of weeks, formal lecture courses, seminar type courses, organized postgraduate programs ranging from one day to several months in duration which are conducted on college campuses, two-week summer sessions on university campuses, seminar sessions of several days, larger group meetings of one or two days and long residence courses at national centers. This study also mentions that almost all of these special programs are self-supporting. Fees are charged which recover all costs.

Probably it will take some time for completion of our study which is now under way, but the foundation has been laid. In the meantime, three courses have been developed, one in report writing, one in accountant's legal responsibility and another in tax practice. The recent announcement made by our Society to give the report writing course to a limited number of our members

resulted in an oversubscription for the course. The year before when this course was offered, the response indicated a considerable amount of disinterest in the course. Possibly our recent experience indicates an increasing interest in continuing education programs.

Self Development

In considering the practitioner's role in developing professional accountants, I would like to discuss first the self-development aspects which apply to all practitioners whether partners, individual practitioners or staff members, and then to comment upon the responsibility of the employing practitioners in developing staff.

Of course, we all espouse the idea of self development, but since we are all busy people it is indeed difficult to find the time to carry out this idea. In this connection, the following quotation from the A.I.C.P.A.'s Bulletin 1, of the Economics of Accounting Practice series on the subject of "Incomes of Practicing Certified Public Accountants," is of interest: ". . . a practitioner may not truly be 'keeping even' with the rest of the world if he commonly works 50 or more hours a week on billable engagements to produce annual income comparable to that of his contemporaries. Without giving sufficient attention to the other activities necessary for professional success, his future growth may be retarded."

It is essential for C.P.A.s to provide time for self development. C.P.A.s must keep up-to-date on matters affecting their work and their profession. One young C.P.A. who started a practice about three years ago in one of our suburbs and is doing exceptionally well, ran into the "lack of time" problem. He solved it by setting aside the hour between 8 and 9 o'clock each morning to review tax services, and read or scan *The Journal of Accountancy*, *The New York Certified Public Accountant*, and releases from professional organizations. He has no set schedule as to what he will read each day, but he is conscientious in devoting that hour daily to "keeping current."

But "keeping current" on matters directly affecting our work or our profession is not enough. We must also keep well informed concerning political, economic, and business conditions on local, national and international levels.

Then again, how many of us know only the financial side of our clients' affairs? Should we not also make it a point to have

an intimate knowledge of their operations, products, and general business problems if we are to be of greatest service?

Do we set aside enough time to take an active part in community and civic affairs as well as in professional activities? Those who do not only enhance their own prestige but also that of the profession. And it is important that in whatever we undertake or do, we have respect for ourselves and for our work. It will also be desirable to cultivate a judicial approach to all problems. Objectivity is at the core of our profession.

Self development has many aspects. Only a few have been mentioned here.

Responsibility for Developing Staff

What is the responsibility of the employing practitioner for developing staff? Relative to this, the following is quoted from a very fine article which appeared in the March 1959 issue of *The Journal of Accountancy*. The title of this article is "Recruitment, Selection, and Training" and the author is our Vice-President, Mr. Samuel J. Duboff. "Each firm has a responsibility for the professional development of every qualified person on its staff so that, if for one reason or another he does not remain with his firm, he will be able to handle himself elsewhere in a manner which is a credit to the firm and the profession."

The way firms carry out this responsibility differs materially, depending on the size of their staffs and their objectives. Most of the larger firms and many of the smaller ones have well organized training programs for beginners and some of them also provide advance courses for more experienced staff members.

Programs for beginners in some cases include classroom training as well as on-the-job training. For example, at L.R.B. & M., our training program for beginners includes six weeks of classroom training. Our training school is held on a college campus in New Jersey and is attended by beginners from our various offices. The instructional staff is composed of partners and staff members. The first four weeks of training, referred to as our Elementary Course, is given each summer for beginners who came with us during the year. Most of the beginners are inexperienced June graduates; the others may have had up to a year's experience. The Advanced Course of two weeks' duration is given the following summer to those who attended the Elementary Course the previous summer.

Unquestionably, classroom training of this kind facilitates the progress of beginners and makes them better representatives of their firms. However, a definite on-the-job training program is even more important. We can safely assume that firms providing classroom training also have well-defined on-the-job training practices. On-the-job training, which provides for rotation of assignments and instruction while carrying out assignments, is equally applicable to small and large firms. To be effective such a program must be formalized so that staff members clearly understand what is expected of them in giving or receiving training. Planned on-the-job training should result in more rapid advancement of staff members.

Probably it is only natural that when staff training is being considered we think first of training for beginners. Of course it is equally important to provide training for staff members at all levels. A number of firms either conduct their own training programs in specialized fields of accounting, in taxes, in S.E.C. matters, in management services, etc., for their experienced staff members or pay the cost of enrolling them in college courses or seminars conducted by professional organizations and others.

Staff training represents a substantial investment. The value of this investment to an employer may be negligible unless staff training is only one part of a good over-all personnel policy. A good personnel policy should include (1) careful selection of beginners, (2) the practice of making advancements from within, and (3) doing those things which create a climate that encourages the retention of staff members.

Selection of Beginners

Careful selection of beginners is the crux of every good personnel policy and, as we know, it is not easy to obtain well-qualified applicants. Although there is no shortage in the number of students graduating with accounting degrees from which to make a selection, there is a definite shortage in quality. This shortage of quality is neither new nor peculiar to our profession. Its effect on us has been to create keen competition among public accounting firms and business organizations for these well-qualified applicants. As a result, such applicants receive several employment offers and, in the last analysis, it is they rather than the employer who make the selection.

I am convinced that these top candidates do not select employers solely on the basis of compensation. They make an objective study of what each employer has to offer and they endeavor to appraise their long-range prospects with the various employers. Training programs, advancement possibilities, the kind of people they will be working with, the diversification of their duties, the amount of travel involved and geographical location enter into their employment decisions. On the other hand, compensation unquestionably does have an important bearing on their decisions when these other factors are fairly comparable. Unfortunately, public accounting in past years has lost many capable students to industry, because of a wide disparity in salaries. However, it is gratifying to note that the disparity is not as great today.

Since professional competence and the quality of services rendered by firms are closely tied in with the caliber of their staffs, the importance of selection becomes readily understandable and an investment in talent takes on clearer meaning. The best source for this talent is the colleges. The national firms which require a large number of beginners each year send representatives to many colleges for recruitment purposes. These representatives interview hundreds of applicants and invite the promising ones to visit their offices, at their firm's expense, for second interviews. Smaller firms which employ only a few men each year would, of course, not find it necessary to have such an intensive recruitment program. However, they should not overlook the possibility of interviewing at a few colleges each year. In this connection, I would like to quote again from Mr. Duboff's article.

> Many practitioners believe that recruitment of outstanding men from the colleges is an area in which they cannot compete with the large firms and I think that they are losing, by default, opportunities to obtain excellent employees. I have interviewed a number of candidates who indicated that they preferred a smaller firm but that the smaller firms were not recruiting on the campus. There are many firms, not national in scope, which can compete quite favorably with the larger firms. The question is not one of size or starting pay only, but rather one of furnishing an environment which challenges a man, meets his needs and expectations and enables him to become a fine professional accountant.

You will note that Mr. Duboff referred to "furnishing an environment" and that earlier in this article, I referred to "creating a climate." What do we mean by these terms and how does one create a favorable climate or furnish an environment? Bulletin 4 of the Economics of Accounting Practice series provides a good

answer. This Bulletin is on the subject of "Getting and Keeping Good Staff Accountants" and to gain background information for this study a survey was conducted. Twenty-five firms, both large and small, located in cities of varying sizes in different parts of the country, were interviewed. The results are summarized and conclusions drawn. The Bulletin emphasizes that the survey is in no sense a statistical study but that the practices presented seem to be indicative of the conditions prevalent within the profession.

The following quotation from Bulletin 4 seems to answer the questions concerning "climate" and "environment."

> One of the urgent problems of the profession is to attract talented young men to its ranks and to retain them when they have gained experience. The approaches of those firms which have been most successful in meeting this problem appear to have these elements in common:
>
> 1. Personal concern for and attention to the staff by the top partners and acceptance of responsibility for helping young accountants to develop.
>
> 2. An understanding of the competitive salary market for college graduates, and a willingness to meet it by subsidizing desirable young men for a year or so.
>
> 3. A systematic program of recruiting, selecting and training.
>
> 4. Tangible and intangible recognition of the individual staff member's work; respect for his personal dignity; treatment of him as a professional even though he may be a beginner.
>
> 5. Planned efforts to provide opportunity for staff members to learn, advance and grow.
>
> 6. A planned program for making other things beside salaries (fringe benefits, working conditions, etc.) reasonably competitive with what others offer outstanding young men.
>
> 7. Aggressive efforts to sell what the practice has to offer, whether the firm is large or small—successful small practices have shown that they can compete effectively in the manpower market.

Conclusion

In concluding this article, I would like to make a few general observations. Those who have been in public accounting for twenty-five or thirty years will recall that even in the early thirties there was some question in the minds of C.P.A.s, themselves, concerning their professional status. We thought and hoped we were in a profession. Some of the accounting literature referred to accounting as a profession but certainly there was little general acceptance of the C.P.A. as a professional man. We have come far in a relatively short time. There is no such question in the minds of C.P.A.s today.

The profession has grown rapidly in size and public acceptance, and it has grown soundly due to the development of its members. There is now every indication of continued growth at a rapid pace, and it is this that emphasizes the need for us to consider seriously our education standards, recruitment practices and development programs, and evaluate them in relation to our future needs. Only by improving the quality of those entering the profession and extending the scope of continuing education for those now practicing public accounting, will we be able to meet our responsibilities and raise the standards and stature of our profession.

Graphics—A Means of Effective Communication*

By M. B. T. Davies (Los Angeles Office)

Man first learned to transmit ideas by making sounds. But the spoken word is difficult to project over distances, and human memory is too frail to make the spoken word a reliable record. So he began to create pictures, and found he was able to project his ideas and messages more dramatically.

As time went by, pictures developed symbolic forms. These became letters and formed the basis of writing through the use of an alphabet. However, pictures are still widely and importantly used. As but a few examples of their effectiveness in gripping the human mind, we see: television and motion pictures—for entertainment and instruction; pictures, charts and diagrams in textbooks—to convey ideas more vividly; illustrations in advertisements—to attract the prospective buyer; illustrated magazines—to portray news in an easily digestible form; and comic strips—to entertain people of all ages.

For many years charts and diagrams have been used copiously in business and professional literature. The reporter finds in them many advantages: he can portray situations more clearly and gain a swifter impact on his reader; he can highlight significant points with more emphasis; he can save reader time; and he can sustain reader interest by varying his illustrative techniques.

The main purpose of a business communication is to help the reader reach a decision. The inclusion of graphics—diagrams, charts or other illustrations—in a business report should also lead to this end. Their use for historical reasons alone should be discouraged; they should be suspect unless they meet the criterion of providing for the reader, alone or as background information, the data he needs for decision-making.

Pointers for Graphic Presentation

Skill and imagination are needed to employ graphics effectively. However, by using some simple aids and principles, the reporter can overcome major pitfalls and convey his message with increased force. Some of these are discussed in the following pages.

* Reprinted by permission from *The New York Certified Public Accountant*, August, 1959, pp. 585–591.

Plan the Story

Charts and diagrams should serve as vehicles in presenting an over-all story. The reporter should outline the story in skeleton form and should study in advance the purpose and effectiveness of each picture he proposes to use. What does the reader need to know? How should the facts be demonstrated? How should the demonstration be fitted into the over-all story? What form of illustration should be displayed? By connecting the facts, by building them into a logical exposition, by illustrating them judiciously and forcefully, the reporter can create an effective message and thereby stimulate action.

Make the Graphics Simple

The human mind absorbs ideas best when they are presented simply and progressively—one at a time. The reporter can economize in space and effort, however, if he conveys several concepts in one picture. While this is easier for him, it is often confusing for the reader, tending to fog his mind, destroy his interest and lose the continuity of the story. Illustrations, therefore, should follow the rule of written language, with facts and ideas unfolding one by one before the reader's eyes. Figure 1 is an example, using the following data:

ANALYSIS OF SALES AND GROSS PROFIT

SALES $000

Product	*A*	*B*	*C*	*Total*
January	100	110	120	330
February	120	130	90	340
March	120	110	90	320
April	140	110	100	350
May	160	100	100	360

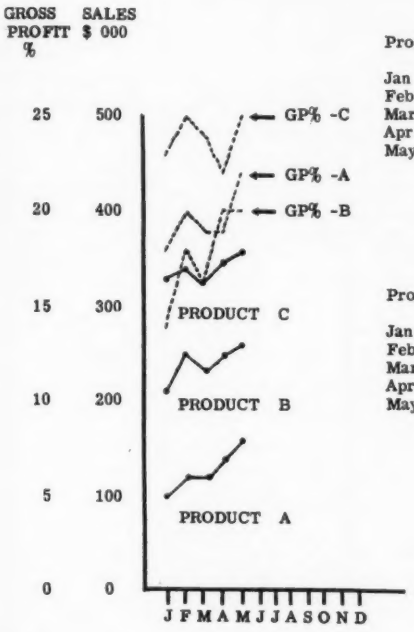
GROSS PROFIT %

Product	*A*	*B*	*C*	*Total*
January	18	14	23	18
February	20	18	25	21
March	19	16	24	19
April	19	20	22	20
May	22	20	25	22

FIGURE 1 Part 1

This chart displays a presentation of sales and gross profit percentages of three related products. Too much information is crowded into one chart. Compactness is achieved at the price of simplicity.

ANALYSIS OF SALES & GROSS PROFIT



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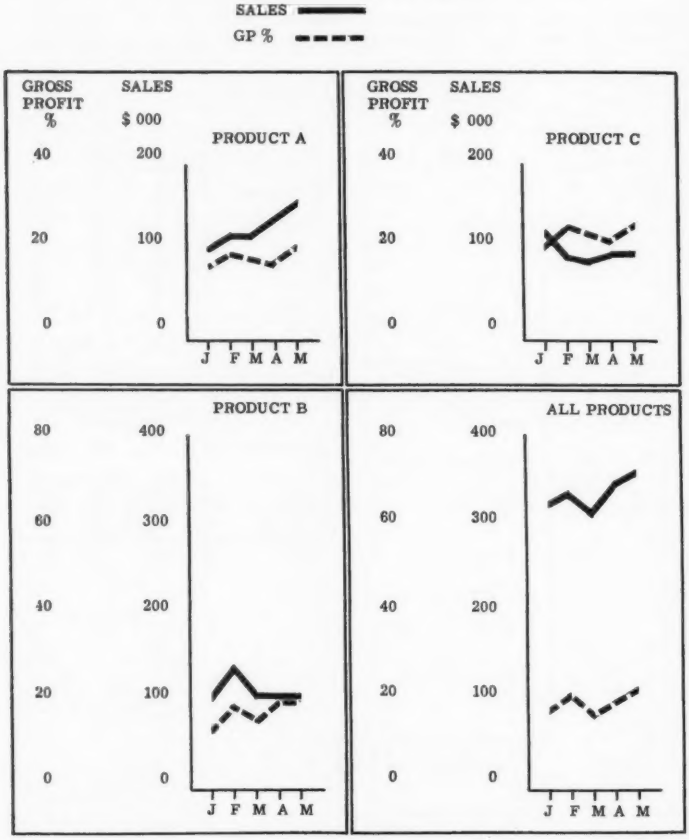
Product	A	B	C	Total
Jan	18	14	23	18
Feb	20	18	25	21
Mar	19	16	24	19
Apr	19	20	22	20
May	22	20	25	22

Select the Best Type of Picture

Many methods of pictorialization are open to the reporter. He should pick the one most suited for illustrating his story. The diagram, in contrast to the chart, demands more skill and imagination because of the wider variety of techniques that can be used. When presenting charts, the reporter should use bars and lines in preference to circles, squares or symbols; one-dimensional straight lines are easier to understand, allow magnitudes to be compared more readily, and offer less risk of misinterpretation.

FIGURE 1 Part 2

The chart shown in Part 1 is here broken down into four individual charts - one for each product and one for the three products combined.



And, while technically it may be more appropriate, logarithmic and semilogarithmic charting should be restricted to the sophisticated reader.

Check for Correctness

In presenting a report that embodies financial and statistical information, the writer will recognize that correctness is of para-

mount importance. When he illustrates the report with charts and diagrams he is faced with another verification task—he needs to be sure that: (1) the basic data are correct; (2) they are correctly plotted and charted; and (3) the illustrations are capable of one interpretation only—the one intended.

Explain the Pictures

Accompanying each illustration in a newspaper or magazine, one generally finds a caption. Contrary to the old adage, every picture does not tell a story; it needs oral or written explanation to support it and explain it. The reporter should, therefore, explain each chart or diagram that he presents, and he may do this in writing or orally, according to his method of presentation.

Where an illustration demonstrates a point of interest, an effective way of highlighting it is to draw attention to it by marking the chart, using a different style of lettering from that displayed in the rest of the chart. Furthermore, in all cases, the illustrations should be used to explain the reasons underlying the facts—the *whys* to support the *whats*.

Limit the Number of Pictures

A graphical presentation can easily develop into a picture gallery rather than an illustrated story. The reporter will generally be well advised to prepare a generous quantity of illustrations in constructing his presentation. He should then review them critically and discard all except those having a significant bearing on the story. The rejected charts should be kept for future use in case of need.

Provide Variety

Reader interest is stimulated by the unexpected and the unusual. Where regular reports are presented at periodic intervals —such as charts of monthly operating results—the subject matter should be varied from time to time to prevent the reports from becoming routine. Similarly, in any one report the pictorial techniques should be mixed, and varying lengths of explanatory matter should be interspersed between the illustrations.

Emphasize the Significant

The reporter will often have individual points of exceptional significance or unusual interest. He will want to impress them

forcefully on his readers, and may use pictorial techniques to do so. A common method of projecting these points is by taking a progressively closer look at the matter in question. The reporter may, as it were, apply a magnifying glass to enlarge the picture; he may increase the magnification step by step; he may shift his sights to an adjoining area to emphasize relationships. With each fresh view he will be drawing the reader's attention more closely and thoroughly to the point he wishes to emphasize. This technique provides a greater variety of perspective by using the "close-up" approach so popular in motion pictures. (An illustration of this technique is contained in Figure 2.)

Time the Presentation

A cardinal principle of reporting is to select the time when the report will have a maximum impact on the reader. Information tends to lose its value as it ages; on the other hand, if reported too soon, the message may be carried to an unreceptive audience. The major purpose of reporting is to assist or influence the audience in making a decision. The person receiving the message may need "pre-conditioning," and the reporter should see that appropriate steps are taken before presenting his story.

Keep the Cost Reasonable

The written or oral report contains two elements of cost—preparation and delivery—the latter including the time of the listeners and viewers. An objective of graphical presentation is to increase preparation costs and gain a more-than-compensating reduction of delivery costs. However, the expense of preparation may become heavy, as it will include: time spent in visualizing and drafting rough charts; time spent in producing, checking, reviewing and finishing the charts; and time and material spent in reproducing and publishing the charts. We have already discussed the need for simplicity and for restricting the number of pictures. Attention to these factors should automatically keep the cost down.

Administration

If a business uses graphic illustration techniques widely, it may be desirable to organize a center to prepare them, produce them and give advice regarding the most effective methods of presentation. Some hints on the conduct of this activity are now discussed. Some of them would apply even if a center is not organized.

FIGURE 2

Illustration of factual development by progressive penetration. (Observe the successive scale changes.)

CHART 1 is a regular monthly chart showing actual costs in comparison with standards. Variances are shown, and an arrow marks the feature needing attention.

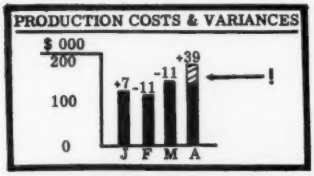


CHART 2 depicts an analysis of variances over a four-month period according to their component parts. The exceptional April feature is now more closely identified.

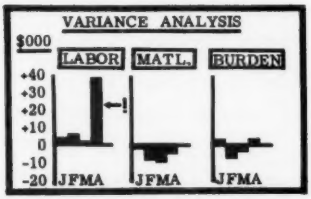
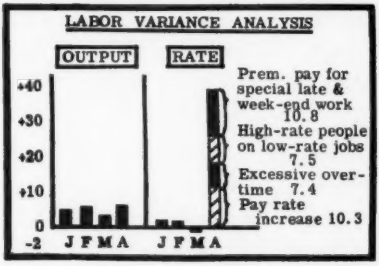


CHART 3 contains a breakdown of the labor variance, identifies the exceptional feature, and breaks it down into further detail.



Program the Output

The center should set up a methodical work program so that its operations can be performed according to logical priorities and without undue strain on its staff.

Use a Job Order System

To keep track of the work expected and that on hand, a job order should be prepared for each assignment. It will thus be easier to program and schedule the work and to accumulate costs where they are needed for record purposes.

Index the Assignments

A card index system may be valuable in forecasting the work involved in regularly recurring assignments and in keeping a compact historical summary of work performed. Each card should contain such data as:

Nature or title of report.	Type of medium used.
Frequency of presentation.	When information is expected.
Originator.	Deadline for completion.

Check the Output

Check lists should be used to make sure that nothing is overlooked and that responsibility is accepted for each phase of the work. The check list may well be combined with the job order record.

Provide Advice in Selecting Media

With the operation of a graphics center, increased attention can be devoted to the quality of output. The center should advise reporters regarding: (1) the effectiveness of their proposed charts, (2) the vehicle best suited for their publication—such as photographic reproduction, slides or easel charts, (3) the expected cost, and (4) the amount of time needed to produce a finished job of the desired quality.

Retain Basic Data

Work sheets, rough charts and other data developed in preparing a presentation should be collected together and preserved. They may be needed by the reporter either to elaborate on his report, including the answering of questions, or to use as a basis for a later report.

Choice of Subject

The accountant has a wide choice of subjects for reporting with the use of graphics. It is not our purpose to consider them here in detail. However, a few typical examples may be of interest.

Flow Charts

Flow charts explain in diagrammatic form the processes involved in performing an operation. Combined with written procedures, they can be valuable for training purposes or for describing a proposed course of work simplification.

Task Charts

The task chart combines a study of: (1) work to be done, (2) responsibilities for its execution, and (3) timing of the work. These charts are particularly valuable for work planning. The "Gantt Chart" is a typical example.

Organization Charts

In addition to depicting responsibilities and reporting relationships, organization charts can be adapted to portray functional relationships, technical liaison, geographical delegation and other features.

Trend Charts

Trend charts, while based on historical data, provide a useful basis for extrapolation and forecasting. Deviations from or changes in trends can be seen at a glance and point immediately to situations calling for management attention.

Performance Charts

The portrayal of results is a standard subject for charting. These are frequently historical only. However, their value can be enhanced by comparing performance with targets, budgets or forecasts, thus identifying at a glance those areas susceptible to management by exception.

In plotting performance, past results should always be corrected to allow for error (for example, incorrect inventory valuations, omissions of accrued expenses, or misclassification of income or costs) even though the double-entry books are not adjusted retroactively. Failure to make these adjustments may cause misleading distortions of information.

Break-Even Charts

The break-even device is a useful tool for determining optimum sales volume or capacity utilization. Through graphical presentation, a more rapid study can be made of relative profitability at selected rates of operation. As such, it provides a guide for management in determining sales and operating policies.

Working Capital Charts

The preservation of a sound working capital position constantly requires close attention. Cash flow forecasts and controls over

receivables and inventories, all of which are protective devices in this area, are particularly suitable for graphic portrayal. Data of these types generally need review at short intervals, and a common practice for transmitting this information is to circulate charts among the interested officials, sometimes enclosed in transparent covers to permit notes and comments to be written on the face of them.

Problem Areas

Conditions of short-lived interest or concern sometimes demand intensive watching, after which they become of routine interest. A stringent cash position, progress on a critical capital expenditure project, installation of a new operation, immediate repercussions of a new course of action—these are but a few examples of features that may attract exceptional attention. Charts providing current reviews at frequent intervals allow these situations to be studied at a glance. (Figure 3 shows a sample of this type of chart.)

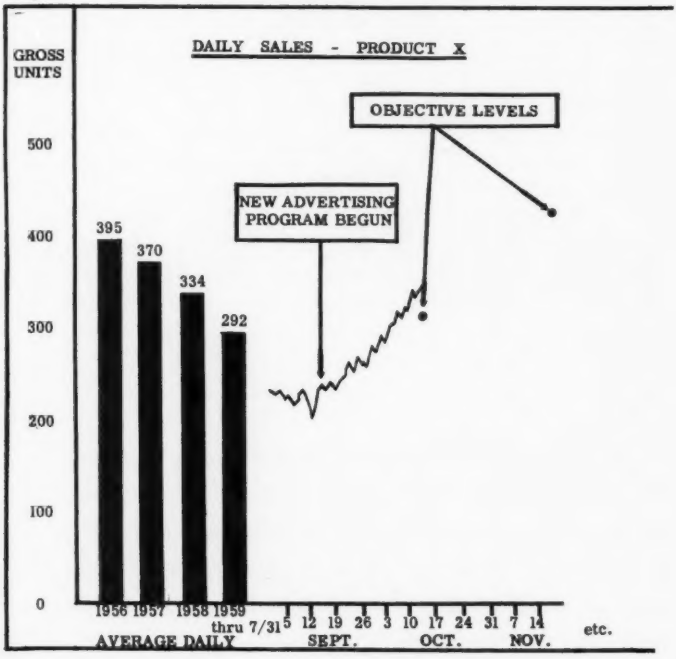
The Accountant's Role

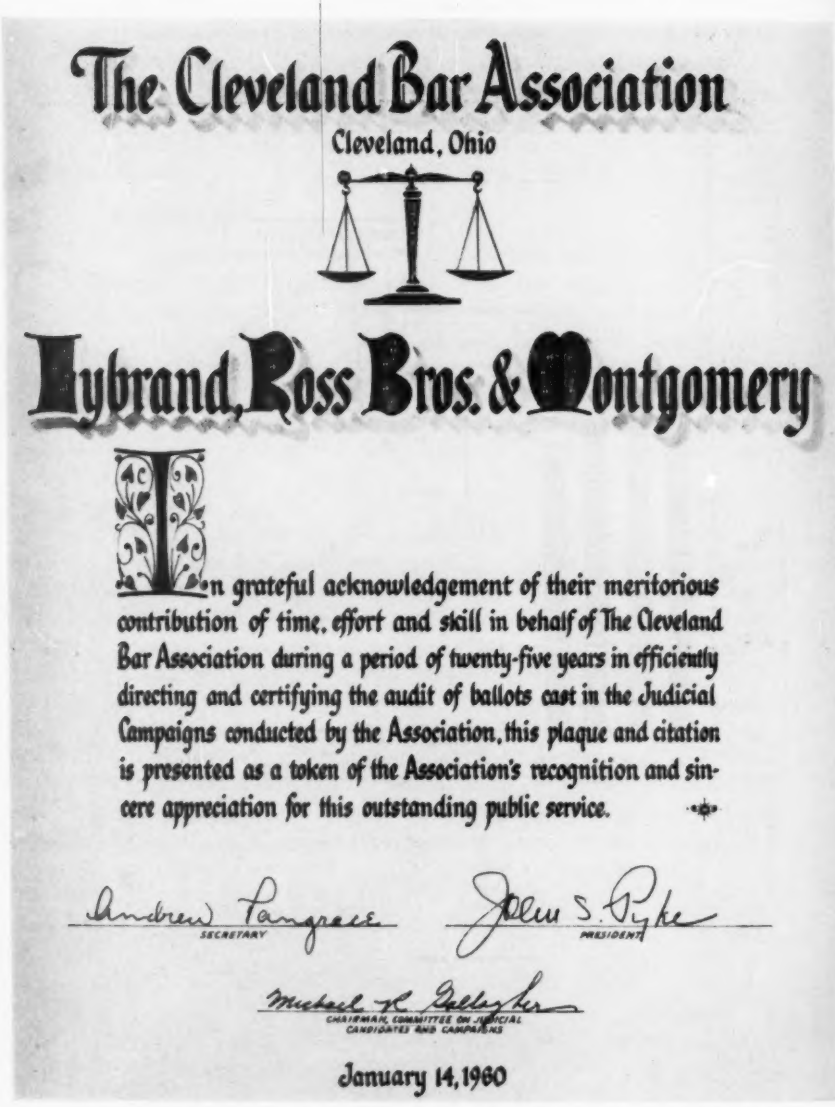
The accountant's task is one of translating events, transactions, operations and conditions into numerical forms and of communicating them in an understandable manner. The use of graphics enables him to communicate with greater clarity and effect. However, he accepts an additional responsibility, first in selecting the graphic methods best suited to support his message, and second in assuring that they neither distort nor conceal the content of the report.

The accountant's position is in no way changed. He has still to portray a statement of the facts; he has still to preserve it from distortion; he has still to transmit it effectively. By adopting graphics as a tool of expression, he needs to change none of his principles, but he has another servant at his command.

FIGURE 3

Example of a chart designed to cover a short-term problem. In this illustration, sales of Product X had progressively declined. An advertising program was started in an endeavor to stimulate sales, and sales objectives were established.





The Cleveland Bar Association

Cleveland, Ohio

Lybrand, Ross Bros. & Montgomery

In grateful acknowledgement of their meritorious contribution of time, effort and skill in behalf of The Cleveland Bar Association during a period of twenty-five years in efficiently directing and certifying the audit of ballots cast in the Judicial Campaigns conducted by the Association, this plaque and citation is presented as a token of the Association's recognition and sincere appreciation for this outstanding public service.

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January 14, 1960

A CITATION RECENTLY AWARDED TO THE CLEVELAND OFFICE

Examinations of Consumer Finance Companies

By Thomas A. Haeussler (*Cincinnati Office*)

A great deal of attention is being given to the tremendous expansion in the use of credit by American consumers. As the use of consumer credit has grown, so have the businesses which supply the credit—the personal credit departments of commercial banks, sales finance companies, small loan companies, etc. The demand for independent auditors who are knowledgeable in this industry has increased correspondingly.

Our concern here is with the companies whose business is primarily the making of small loans. These companies operate under the small loan laws of the respective states in which their branches are located. The laws vary somewhat from state to state, but all are rather restrictive in their provisions. The laws set forth, among other things, the maximum interest rates, the maximum amount that may be loaned to one customer, and the types of security permissible. Maximum loan amounts vary from $200 in some states to $5,000 in others. Interest rates are generally on a sliding scale depending upon the size of the loan. For example, in Ohio the maximum interest rate on small loans is three per cent per month on the first $150, two per cent per month on the next $150 and eight per cent per annum on amounts over $300 to $1,000. The loans may be secured by chattel mortgages on household goods, automobiles, farm equipment, trailers, boats, etc., and by wage assignments or they may be unsecured signature loans. The loans may also have the signature of a co-maker on the note.

The small loan companies operate through a number of branch offices. These branches may have more than one corporation operating within the office, and a number of the branches may themselves be separate subsidiary corporations. The larger companies operate through hundreds of branch offices and a correspondingly large number of corporations.

Small loan companies may also have licenses to buy sales finance contracts and to make wholesale or floor plan loans to dealers. Sales finance companies may also have licenses to make small loans. The differentiation generally made between the two

types of companies is on the basis of the company's major activity. That is, small loan companies derive most of their income from small loans and a lesser amount from their sales finance business.

In the following paragraphs certain accounting and auditing problems peculiar to the typical small loan business are considered in the order in which they are encountered in the financial statements.

Cash: The cash accounts in a small loan company are quite numerous, as they are in any chain operation. There will be at least one fund of cash on hand and one bank account in each branch office. There may be more if more than one corporation is operating in the branches. Also, there will be petty cash funds and operating bank accounts in the home office and inactive bank accounts in which reciprocal balances on bank lines of credit are maintained.

A large amount of audit time can be spent on the examination of these accounts with little justification, since the cash in the branch and home office bank accounts generally is a relatively small part of the company's total assets. The time required to examine the cash accounts can be materially reduced, provided internal check and control is satisfactory, through examining selected accounts on a test basis, and reviewing the company's reconciliations on the others.

Loans Receivable: The majority of small loans are made to persons in the lower income groups. These people are generally unfamiliar with business customs; specifically, they are unfamiliar with requests for confirmation from independent auditors. As a result, if positive type confirmation requests are mailed, the response is highly unsatisfactory. The debtors either do not understand the request being made of them or do not care to exert themselves sufficiently to return the confirmation form. It is, therefore, a waste of effort to use positive type requests. The better policy is to send negative type requests to a larger number of debtors.

The confirmation request form should state as clearly and simply as possible the request that is being made. The client's name must be prominently displayed or the customer frequently becomes confused and thinks his account is with the auditing firm. A statement to the effect that the letter is not a request for payment should also be shown prominently.

The investigation of the confirmations returned with differences reported by the customer, those returned by the post office, and of accounts on which the customer has requested that no mail be sent is very difficult for the auditor since the records and customers are, in general, widely spread geographically. The cost of the investigation of these accounts by the independent auditors themselves would be prohibitive. A satisfactory substitute is for the internal audit group to investigate these accounts on their periodic trips to the branches and report the results of their investigations to the independent auditors. The independent auditors can then make such additional examination and confirmation as they deem to be necessary.

Allowance for Uncollectible Loans: This account is of major importance in a small loan company for two reasons: The comparatively greater credit risk assumed in this type of loan and the fact that loans receivable comprise a very high percentage of the company's assets.

There are two viewpoints concerning these allowances or reserves. . . . One is the traditional accounting viewpoint that such a reserve is a valuation reserve intended to recognize that the loans outstanding at any given date include uncollectible accounts for which a reserve should be established to reduce the loan balances to an estimated realizable amount. The other viewpoint is that these reserves are not only valuation reserves, but are also reserves against economic declines and, as such, should include an additional provision to take care of losses due to such economic problems. The latter viewpoint is frequently encouraged by the company's creditors who, adopting the traditionally conservative approach, feel more secure with the presence of large reserves for losses on the balance sheet.

The generally accepted practice in the industry is to show the allowance for uncollectible loans as a reduction of receivables whether its amount is determined under the first or the second of the above two theories. If the allowance is determined under the second theory, it would seem that the auditor should decide whether the excess allowances, that is, the amount of the reserve in excess of the amounts justified by experience, is sufficiently material to require presentation as a reserve for contingencies rather than a valuation reserve.

The auditing problem encountered on this account is, of course, the determination of the adequacy of the allowance at the balance

sheet date. To do this, the auditor must review the company's method of charging off uncollectible loans. He will want to know whether the company automatically charges off loans after a stated period without payments; whether the company keeps the loan on its books until there is absolutely no doubt that it is uncollectible; or whether some intermediate course is followed. A review of the actual charge-offs must be made to see that the stated policy is being followed. The auditor should also review the company's delinquency statistics and compare them to the reserve at the balance sheet date.

One of the most helpful procedures in assisting the auditor in forming his opinion on the allowance for uncollectible loans is a summary showing the relationship of the allowance required at previous balance sheet dates to the receivables at those dates. This can be accomplished through an analysis of each of the past 10 or 15 years' charge-offs by the year in which the loans were made. After determining the total dollar amount of loans made in one year or earlier and charged off in subsequent years, the amount of reserve required at the end of that year is known. This required reserve can then be stated as a percentage of the loans outstanding at the end of that year. If this is done for each of the past five or ten years, the auditor can see how the percentage at the current balance sheet date compares to the percentage at previous balance sheet dates.

A weighting of the more current years' experience will have to be made, since all of the bad accounts will not yet be charged off at the current balance sheet date. The last bad accounts may not be charged off until five, six or seven years after the loan is made. This weighting can be accomplished through an analysis of the early years' experience on the amount of loans charged off in the first, second, third, fourth and fifth years after the loans were made.

Since the time involved in preparing this computation is quite lengthy, the client should be requested to prepare this summary. The company can also use the summary as substantiation of its deduction for federal income tax purposes.

Unearned Discount: This account is of more importance in a sales finance company than in a small loan company. Since small loan companies generally have some sales finance accounts and since some states are permitting a type of small loan with the

interest precomputed in the loan balance, the account is discussed here.

Unearned discount arises when a finance company purchases a sales finance contract from an appliance dealer, automobile dealer, etc., or makes a direct loan on a discount basis. The entry recording the unearned discount (disregarding fees, dealers' holdbacks and reserves, etc.) is a charge to loans receivable, a credit to cash, and a credit to unearned discount for the difference between the cash paid-out and the amount to be repaid by the debtor.

Two methods of absorbing unearned discount into income are in use:

1. Recording the proportionate part of the actual payments received that represents discount (cash basis).

2. Recording the discount earned as a result of elapsed time rather than as a result of payments received (accrual basis).

The first method is more frequently used by the larger companies than is the second. In either case tests of these accounts can be made with relative ease by the auditor.

Some companies, generally smaller ones, reverse the above procedure by crediting all discount to earned discount when the paper is purchased and setting up the unearned portion at each balance sheet date.

Some of the methods used in computing the earned and unearned portions of the finance charges are:

1. Using the "rule of 78" which is a sum of the year's digits approach in which 12/78 of the unearned discount is taken into income the first month, 11/78 the second month, and so on;

2. Computing the percentage that unearned discount is of outstanding sales finance receivables at the first of the month and applying this percentage to the payments received during the month to secure an earned discount figure; and

3. The use of a fixed percentage of outstanding receivables for unearned discount at each balance sheet date.

The last approach is undesirable from an accounting viewpoint since it does not necessarily have any basis in fact and distorts the earned and unearned figures.

Repossessions: This account applies only to the sales finance business done by the small loan company, and is carried on its books in accordance with one of two methods: at loan balances or at the lower of the loan balance or current market price of the item repossessed. The latter method is preferable.

This account is generally an insignificant one in the balance sheet.

Deferred Development Costs: Some companies in the consumer finance industry defer the operating losses arising during the first months of operation of a new branch office. These deferred charges are then written off against income over an arbitrary period such as five years.

This practice has been condemned by some as being contrary to the objective of properly determining net income through the matching of applicable costs and expenses against revenues. These persons advocate that such operating losses should be charged off as incurred in order to conform with generally accepted accounting principles. However, since the practice of deferring initial operating losses of new branches is apparently so widespread in the industry it is considered equally acceptable.

Dealer Holdbacks and Reserves: In connection with any sales finance activities of the company there will also be dealer holdbacks and reserves arising from the arrangements made with the dealers for purchasing sales finance contracts from them. Holdbacks and reserves are amounts retained by the finance company at the time the contract is purchased from the dealer and are paid later to the dealer when certain specified conditions or events occur. Holdbacks represent a portion of the financed amount which is held back to cover losses in case of repossession. The reserves are really commissions to the dealer for giving his business to the finance company. The holdbacks are paid to the dealer when the contract is paid off by the customer. The reserves may be accumulated until they reach an agreed percentage of the dealer's customers' balances depending upon the contract with the dealer. They are adjusted for refunds of finance charges if the customer pays the loan before its maturity date and for bad debt and repossession losses. Periodic payments are made to the dealer of amounts in excess of the agreed upon percentage.

Where holdbacks and reserves are a significant figure, confirmation of the balances may be secured from the dealers. The transactions in the accounts can be tested with relative ease.

Interest Income: Interest income may be recorded either as received from customers or as earned as a result of elapsed time. Generally the larger companies report interest income as payments are received.

Tests of the recorded interest income may be made by selecting various days' payment reports, checking the recorded interest against printed interest tables, and tracing the entries into the records.

Expenses: Some companies consistently report expenses, except income taxes, as paid rather than as accrued. Income taxes are reported on an accrual basis. The auditor must determine whether the distortion resulting from the use of this hybrid method of accounting is material before expressing his opinion on the financial statements. Generally the unrecorded income more than offsets the unrecorded expenses.

Internal Control: A system of internal check and control, appropriate to this type of operation, is essential in consumer finance companies where large amounts of cash are readily available and only one or two persons are involved in a complete transaction in the branch office.

The auditor can render a valuable service to his client through recommendations for improvements in the system of internal check and control, and his review of the system as part of his audit procedures will afford him an excellent opportunity to observe areas in which such improvements can be made.

Budgeting and Forecasting*

By Robert L. Burton (*New York Office*)

Budgeting and forecasting do not have to be explained or "sold" to the management of any well-run business or nonprofit organization. While these familiar tools of effective control have wide acceptance, it is surprising that even some major corporations do not make full use of their capabilities. The neatly bound and meticulously prepared budgets that one frequently sees are not always used for planning and control. Instead, management decisions are sometimes made without consideration of the effect on the budget or the over-all operating plan. This does not mean that management should relinquish its prerogative to take action necessitated by changing times or conditions in order to stay within the limits imposed by inflexible budgets. Rather, the forecast and budget, when compared with the results of actual operations, should serve as guides to management when making important decisions.

The forecast and budget should be reviewed periodically. Many companies do so quarterly. Revisions must be made to conform the budget and forecast to major changes authorized by management. The budget and forecast should always represent the best estimate of potential volume and the most effective plan for using the organization's available resources to maximize profits. In the case of nonprofit organizations, the desired goal is to get maximum use out of revenues while keeping administrative costs to a minimum.

One should not make the mistake of considering budgets and forecasts as being essential only to large or medium-sized organizations. While it is true that the small businessman usually is conversant with the potentials and problems of his business, the use of budgeting and forecasting is just as essential to the continued successful operation of a small business as to its larger competitors. The small business does not require a highly sophisticated type of forecast and budget. The installation of practical budgeting procedures is another area where public accountants can render invaluable service to their smaller clients.

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Budget Planning

Historical data, notably the results of operations in past periods, provide basic information for the forecast and budget. Although these data are important, it is also imperative that future prospects be considered. Very few business organizations have achieved any real success by constantly looking backward, and no human being has the power to infallibly forecast the future. However, techniques developed by economists, statisticians, market researchers and others have tended to dispel some of the haze that always surrounds future predictions.

It is essential, when establishing a budget that both short-term fluctuations and long-term trends be considered. Short-term fluctuations (for example, the duration of a business recession and its effect on a particular industry) are quite difficult to gauge. The recession that occurred during 1958 is a prime example. Some industries experienced severe declines in sales volume and profits. Others were unaffected. Still others enjoyed increased volume and profits. The recession affected some geographical areas of the country far more than others. How does one weigh in all of the complex factors that might affect the future course of a business? There is no simple answer; the best available method uses past operating results, takes into account the expected impact of short-term economic factors, weighs the potential effect of trends in the industry, and utilizes the best available data resulting from market and product research. The work of operations research teams in some major companies assists management in coping with the many variables involved. In smaller organizations, reliance must be placed upon the judgment of the management team.

Master Budget

An over-all plan must be developed to establish the desired goals and the methods of attaining them. That is the purpose of the master budget.

The logical starting point is the sales forecast, or, for nonprofit organizations, the estimated revenues. The sales executives of the organization obviously must supply their estimates of the sales volume. Since all other aspects of the budget are dependent upon this forecast, it is imperative that it be reasonably accurate. Sales executives are basically optimistic and it is incumbent upon the budget committee and the budget director to assure themselves that this optimism has not unduly influenced the sales forecast.

Inflated sales forecasts can and usually do mean that the organization will incur a lot of needless expense. Overbuying and overproduction, excessive inventories and unwarranted carrying charges, increased personnel costs, and a host of other unjustified expenses can result.

Once the expected sales volume has been established, each of the other aspects of the company's operations can be considered and requirements determined. How large an inventory will be needed, what purchases will have to be made, how much will have to be produced, how many employees will be hired or terminated? The answers to these and to many other questions must come from an evaluation of the sales forecast.

The master budget represents the over-all "profit plan" that management uses for control purposes. From it stem all of the other types of budgets that are discussed in subsequent sections of this article.

Sales Budget

The sales budget provides the details necessary for preparing the forecast sales section of the master budget just described. It is important that the most advantageous product mix be determined. (Product mix is that volume of sales of each of the products in the company's line that will return the best profit consistent with prevailing conditions.) Accordingly, the sales forecast is developed by product and product line which provides the data necessary for preparing the purchasing and production budgets.

Another important aspect of the sales budget is the assignment of sales quotas to various organizational units comprising the sales department. Therefore, the quotas set for individual salesmen, sales offices, etc., must be incorporated into the over-all sales budget. The attainment of the desired sales volume hinges largely upon the ability of the sales personnel to produce. The expenses to be incurred in connection with the direct sales effort must be decided upon for incorporation in the sales expense budget.

Sales Expense Budgets

How much must the organization expect to spend to produce the desired sales volume? Obviously, the answer is to spend enough to provide incentive to the members of the sales force to attain or better the established quotas. Here, again, a very important point must be kept in mind. The sales incentive must be worked out

in such a way that the desired product mix is attained. It quite often happens that those products that produce the smallest profits are also easiest to sell. Enlightened sales management certainly takes that into account when establishing the sales quotas and related incentives.

The elements of direct selling expenses must be provided for. Salesmen's salaries, commissions and expenses have to be keyed to the volume that the members of the sales force are expected to produce. The cost to the company must be measured in terms of sales volume. The various organizational units assigned by geographical area, product line, or other categories must be allocated a portion of the over-all selling expense budget consistent with the quota requirements.

In effect the sales expense budget must be developed along two separate lines. The desired product mix must be introduced into the quotas that are set up and the anticipated selling expenses to produce the desired volume must be determined. It is incumbent upon those responsible for budget preparation to allocate the allowable expenses by organizational units.

Comparison of actual selling expenses with the budget should be made with a view toward determining that the expenses incurred have resulted in the production of sales volume consistent with management's established goals. Obviously, in only a few instances is it possible for sales forces to produce business in exactly the volume and product mix that are considered desirable by management. The comparison between actual selling expenses and those budgeted must be made in the light of the ability of an organizational unit to provide the desired volume within the framework of the budget established for it.

Many small organizations include sales promotion and advertising in their selling expense budgets. For the purpose of this article, sales promotion and advertising expenses will be considered as belonging to separate budget classifications. The importance of these two types of expenses in the light of present competitive conditions certainly warrants that they should be controlled separately.

Production Budget

It is quite obvious that the production budget is associated solely with manufacturing enterprises. When preparing this budget quite a number of factors must be considered. The sales

forecast, again, is a major consideration. The product mix that has been established as the result of preparing the sales budget must control. The quantities that are presently on hand in the raw material, work-in-process or finished state must be considered. The ability of the production facilities of the organization to produce the desired quantities and quality of products has to be weighed. Perhaps it is most economical to buy a product either partially finished or to have it completed by a vendor; "make or buy" decisions must be made. Model and style changes must be provided for. Personnel and equipment requirements have to be taken into account. Tooling requirements are essential considerations. The quantities of raw materials, semifinished parts, supplies, etc., must be determined for the purpose of preparing the purchasing budget. Coordination of all of the rather complex aspects of the production budget with the various other types of budgets can be a formidable job, particularly in a major manufacturing company with a large number of products and diversified product lines.

The preparation of the production budget calls for team action. The production executives, engineers, managers and other members of the production force must provide their estimates of all the requirements outlined above. These must be reduced to the common denominator, dollars, which is usually developed in cooperation with the budget director or his staff.

The production budget further affects the cost accounting department. The determination of labor and burden rates must be consistent with the budgetary requirements.

For those companies using standard costs, standards sometimes have to be revised. For new products and model or style changes, it is essential that up-to-date standard costs be established.

Comparisons of actual production costs with the budgeted costs must be made in the light of variance from established standards or deviations from budgeted goals. This provides the measure for determining the reasons for not meeting production goals. Variance analyses point up the reasons and clearly fix responsibility. Price, usage, volume and performance variance enable management to gauge the efficiency of the production operation and the effect upon cost of sales.

Adjustment of production budgets must be made periodically. Usually such adjustments result from the negotiations of labor contracts, substantial price or volume changes, etc. Technological

improvements made during a period to which a budget applies frequently have a substantial effect upon the manufacturing costs. The budget for the remainder of the period obviously must be adjusted to give effect to the changed situation.

Purchasing Budget

The smooth functioning of any manufacturing or mercantile business depends to a large extent upon the availability of inventories. Both out-of-stock or overstocked conditions are dangerous. The first usually means loss of business and delays in production scheduling. The latter incurs a lot of unnecessary costs. These costs include excessive inventory carrying charges, increased warehousing expenses, greater chances of spoilage or deterioration, obsolescence necessitating markdowns or other disposal, and a host of other unnecessary costs.

It is incumbent upon top management to define the parameters within which the purchasing units must operate. The purchasing function must be keyed to the requirements of all phases of the company's operations. Maxima should be established for inventory investment. With company policy firmly established, the purchasing executives can then develop the overall program for their departments. Lead times, availability of materials or merchandise, cyclical fluctuation, requirements consistent with economic ordering quantities, and all the other factors that affect the purchasing program must be considered.

The requirements of the purchasing budget and forecast must be keyed to the financial budget. Since a considerable portion of the accounts payable of a business usually arises from inventory purchases, it is essential that financial management be provided with a forecast of cash requirements to meet such obligations. Often this entails establishing substantial lines of credit to finance purchases. This further points up the need for the coordination of all phases of the company's operations through the master budget.

As in the case of the production budget, the purchasing budget must be revised on occasion to give effect to changes in business conditions. Expected major price advances may make it desirable to hedge by increasing the investment in inventory. On the other hand, substantial price reductions may make it advantageous to reduce inventory levels to a safe operating minimum. Top management must be alerted to the possible impact of major price fluctuations in order to plan any changes in the purchasing budget.

Expense Budgets

Except for the sales expense budget, which was discussed previously, all types of expense budgets will be covered in this section. Basically, there are two types of expense budgets—departmental and functional.

Departmental budgets provide for all types of expenditures that are likely to be encountered by any organizational unit. These include salaries, wages, supplies, taxes and the entire gamut of operating expenses. The budget appropriates an amount sufficient to cover the anticipated expenses to be incurred in connection with the workload that will be handled by the organizational unit. Again, the sales forecast, as contained in the master budget, determines the level at which each department will operate. The personnel, equipment, space requirements and all other considerations hinge upon the anticipated volume of business to be transacted. It is incumbent upon the department head to live within his budget or to have good justification for requesting an increase in appropriation. Conversely, good management on the part of a department head may enable him to effect savings. The ability of a department head is normally evaluated on the basis of the performance of his unit. A further test of his managerial skill is his ability to operate his unit at a cost not in excess of the budget authorization. Except for special costs, of which top management would certainly be aware, the departmental budget should reasonably approximate the actual expenses.

Functional budgets enable management to control the various types of natural expenses. Advertising, sales promotion, research and development are notable examples of this type of budget. Obviously, management desires to get the maximum benefit from expenditures of this type. Effective control to assure that the cost is kept to a minimum consistent with the over-all profit plan must be maintained. A percentage of forecast net sales is used by many companies as the basis for establishing the advertising and sales promotion budgets. Research and development budgets are usually geared to the long-term program of the organization. The development of new products, improvement of existing products, development of new types of production machines and equipment must all be identified with the future program of the company. In a dynamic organization it is imperative that the present be used to prepare for the future. Otherwise stagnation sets in, which ultimately can cause the organization to fail.

The advertising budget usually controls the expenditures of relatively substantial sums of money. Still, the benefits derived from advertising are among the most difficult to appraise. The effectiveness of an advertising program can only be judged by the fluctuations in sales volume. It is extremely difficult to identify the results of an advertising campaign with sales dollars. Many other factors may also influence sales. Therefore, the control of the dollars expended for advertising must be made as tight as possible to minimize cost. There are few organizations that can get along without advertising; the intangible benefits derived from it must be identified with some tangible results of operations. Again, advertising campaigns do not always produce immediate results. Often long after an advertising campaign has terminated, the benefits continue to be realized.

It is customary, particularly with major advertising budgets, to place the responsibility for the over-all program with an advertising agency. Reliance must be placed on the artistic, technical, and creative skills of the agency's staff. The only tangible results of the advertising program are the copy that appears in various printed media, on billboards, or on the programs or spot announcements that are broadcast on radio or television. Management must evaluate the effectiveness of the advertising on the basis of the sales volume and the advertising cost per sales dollar to produce that volume.

The results obtained by incurring sales promotion expense are somewhat easier to gauge than those pertaining to advertising. However, there still are many nebulous areas that must be considered here. Again, as in the case of advertising, the best method to determine the success of a sales promotion campaign is the increased volume of sales produced as a result. Is the cost of sales promotion justified in terms of the total sales produced, or, better still, has the net profit of the company increased because of the sales promotion effort? Comparison of the sales promotion costs with the actual sales and the ultimate net profit is the only really reliable measure.

Capital Expenditures Budget

Every business organization must have property, plant and equipment in order to operate. Replacements of or additions to these assets customarily require careful planning over long periods of time. The cost of new facilities is usually substantial, which

obviously poses the problem of how financing will be accomplished. Then there is the time factor; new facilities must be planned long in advance in order to have them available when needed. Accordingly, trends in the industry as well as the forecast of the organization's share in the potential market must be considered. Technological advances in many industries have made it mandatory that equipment be replaced with more sophisticated or later model equipment in order to keep costs down and to maintain a favorable competitive position. Many variable factors have to be weighed before decisions can be made.

The capital expenditures budget provides for the preliminary studies essential to the formulation of plans for ultimate acquisition of property, plant and equipment. It also gives effect to the current program of construction and acquisition. The current year's requirements for capital expenditures as well as the provision for future years' programs are important to any progressive business organization in order to assure its continued successful operation.

While the stress in this section of the article has been placed upon the programs of profit-motivated business organizations, it is equally important that nonprofit organizations also recognize the importance of the capital expenditure budget. The same factors influence the decisions that must be made by directors or trustees relative to capital acquisitions. Programs for providing new property, plant and equipment must be considered well in advance of the time of need for the facilities. Coordination of these plans with fund raising is essential to the successful culmination of any program for expansion or replacement.

Financial Budgets

Few business or nonprofit organizations are in the happy position that they do not have to carefully forecast their cash requirements. The few organizations that do not have to consider this problem usually have reached that position by careful financial budgeting in prior periods.

The forecast of cash receipts and cash requirements in the immediate future and for the long term are essential to the proper administration of the company's or organization's affairs. Financial executives must lean heavily on the forecast of financial resources and requirements of their organizations in order to plan effective financing or to call for additional investment by owners and stockholders or for additional contributions from donors.

Financing poses the problem of interest costs and the impact that such costs will have upon the net profits of future periods. Once the indebtedness has been incurred, it is mandatory that provision be made for the amortization of the principal balance of the loan as well as for the interest payments due on the unpaid principal balance.

Coordination of all aspects of anticipated cash receipts and cash disbursements is essential to financial budgeting. It is necessary that the pattern of remittances from customers or donors be determined so that the cash inflow may be correlated with cash requirements. Careful planning and control minimizes the need for short-term borrowing in order to meet current financial obligations.

It is a waste of time to prepare a cash forecast and then permit it to fall into disuse. Unfortunately, this sometimes happens. Instead of carefully comparing actual cash receipts and disbursements with the cash forecast, some financial executives work entirely with the actual figures. Certainly, the actual figures are by far the most important, but for planning purposes the forecast must be adjusted to reflect the anticipated requirements for the immediate future and the long term. It is too late to plan a financial program when the cash requirement has arisen. Therefore, enlightened financial management avoids this pitfall by advance planning through the financial budget.

Awards and Prizes

THE PRIZE-WINNING ARTICLES FOR 1959

The Firm is pleased to announce the awards for the best manuscripts by staff members published during 1959 in *The Journal of Accountancy*, the *Lybrand Journal* and other technical magazines and journals.

The Journal of Accountancy:

FIRST PRIZE—$1,000. Awarded to CLIFFORD W. STOWE for his article entitled "Moral Responsibility in Tax Practice."

Lybrand Journal:

FIRST PRIZE—$1,000. Awarded to DR. MICHAEL SHEGDA for his article entitled "Management Action and Planning for Successful EDP Installation."

SECOND PRIZE—$500. Awarded to J. WALKER VORIS for his article entitled "Cost Consciousness Through Cost Control."

Other Publications:

FIRST PRIZE—$1,000. Awarded to DR. FELIX KAUFMAN for his article entitled "EDP and the Disenchanted" which appeared in *The California Management Review.*

SECOND PRIZE—$500. Awarded to Stanley C. Simon for his article entitled "Supreme Court Says No to Capital Gain Treatment of Carved-Out Oil Payments" which appeared in *Taxes.*

Electronic Data Processing—Subject Bibliography of Periodical Literature, 1959*

The rapid acceptance of electronic data processing equipment has given rise to a corresponding growth of periodical literature relating to all phases of EDP. The Firm's Management Services Research Staff has prepared this subject bibliography for those who may be interested in articles reporting current EDP trends and procedures.

Approximately seventy-five periodicals published during the calendar year 1959 have been reviewed, and articles of general interest in the field of electronic data processing have been selected. Articles dealing primarily with specifications of manufacturers' equipment have been excluded since such specifications are included in the Lybrand publication and updating service "EDP Equipment Characteristics."

The selected articles have been classified according to subject only, and within a given subject category alphabetically by title. Where several subjects were covered in an article its title is repeated under each pertinent heading.

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23 Essex St.
London W. C. 2

The Accounting Review
R. Carson Cox
College of Commerce
Ohio State University
Columbus 10, Ohio

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Dartnell Building
4660 Ravenswood Ave.
Chicago 40, Ill.

American Gas Association Monthly
420 Lexington Ave.
New York 17, N. Y.

The Arthur Andersen Chronicle Editor
120 South LaSalle St.
Chicago 3, Ill.

Arthur Young Journal
Frederick E. Horn, Editor
165 Broadway
New York, N. Y.

Auditgram
38 S. Dearborn St.
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Automatic Data Processing Service Newsletter
John Diebold & Associates, Inc.
40 Wall St.
New York, N. Y.

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12 East 36th St.
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Best's Insurance News, Fire and Casualty Edition
Alfred M. Best Company, Inc.
75 Fulton St.
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Alfred M. Best Company, Inc.
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New York 38, N. Y.

Business Horizons
School of Business
Indiana University
Bloomington, Ind.

Business Week
McGraw-Hill Building
330 West 42nd St.
New York 36, N. Y.

California Management Review
Graduate School of Business Administration
University of California
Los Angeles 24, Calif.

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69 Bloor St. East
Toronto 5, Canada

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Editorial and Executive Office
2 Park Ave.
New York 16, N. Y.

The Chartered Accountant in Australia
The Editor
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Box 3921, G.P.O.
Sydney, N.S.W.

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American Chemical Society
20th and Northampton Sts
Easton, Pa.

Communications of the Association for Computing Machinery
2 East 63rd St.
New York 21, N. Y.

Computers and Automation
Berkeley Enterprises, Inc.
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Newtonville 60, Mass.

Computing News
Box 261
Thousand Oaks, California

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McGraw-Hill Building
330 West 42nd St.
New York 36, N. Y.

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229 Park Ave., So.
New York 3, N. Y.

Datamation
141 East 44th St.
New York 17, N. Y.

Dun's Review and Modern Industry
99 Church St.
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Electronic News
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7 East 12th St.
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New York 22, N. Y.

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270 Madison Ave.
New York 16, N. Y.

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Association for Computing Machinery
2 East 63rd St.
New York 21, N. Y.

The Journal of Industrial Engineering
A. French Building
225 North Ave., N.W.
Atlanta 13, Ga.

Journal of Machine Accounting
NMAA National Headquarters
208 South Main St.
Paris, Ill.

Lybrand Journal
Lybrand, Ross Bros. & Montgomery
2 Broadway
New York 4, N. Y.

Machine Accounting and Data Processing
270 Madison Ave.
New York 16, N. Y.

Management and Business Automation
600 W. Jackson Blvd.
Chicago 6, Ill.

Management Methods
22 West Putnam Ave.
Greenwich, Conn.

The Management Review
American Management Association, Inc.
1515 Broadway
Times Square
New York 36, N. Y.

Management Science
Harold H. Cauvet, Business Manager
P.O. Box 273
Pleasantville, N. Y.

Modern Railroads
Watson Publications, Inc.
201 North Wells St.
Chicago 6, Ill.

N.A.A. Bulletin
National Association of Accountants
505 Park Ave.
New York 22, N. Y.

Nation's Business
1615 H St., N.W.
Washington 6, D. C.

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Navy Management Office
Room 0137, Main Navy Bldg.
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355 Lexington Ave.
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Office Publications, Inc.
232 Madison Ave.
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212 Fifth Ave.
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211 S. Cheyenne
Tulsa 3, Okla.

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56 Pine St.
New York 5, N. Y.

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270 Madison Ave.
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Retail Control
Controllers' Congress N.R.M.A.
100 West 31st St.
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100 West 31st St.
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Remington Rand
315 Park Ave., So.
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4463 Penobscot Bldg.
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Speaking Engagements

Date	*Speaker*	*Organization*	*Topic*
Jan.			
4	William W. Ragsdale, Jr. Birmingham	N.A.A., Birmingham Chapter	TV Panel Discussion. The Accountant Today
6	Joseph E. Tansill, Chicago	Controllers Institute, South Bend	Recent Trends in Taxation
8	Louis S. Sorbo, Louisville	Medical Service Society of America, Jeffersonville, Ind.	Income Taxes
12	Robert C. Gray, Cincinnati	Cincinnati Credit Club	Panel Member—Individual Income Taxes
12	C. John McDowell, San Francisco	Bankers-C.P.A.s Seminar, San Francisco	Discussion Leader
12	Donald W. Schroeder, San Francisco	Bankers-C.P.A.s Seminar, San Francisco	Skit—Inside Montgomery Street
12	Herman Stuetzer, Jr. Boston	Norwell Lions Club	Business Expense Deductions
16	Kenneth J. Mutzel, Philadelphia	National Electronics Distributors Association, Keystone Chapter, Camden, N. J.	Maximizing Net After Taxes
18	Herman Stuetzer, Jr. Boston	Tax Executives Institute, Boston Chapter	Massachusetts Corporation Excise
19	Tibor Fabian, M. S. R. & C. D.	American Management Association, New York	Proper Balance Between Maintenance and Replacement
19	Robert S. Haas, Philadelphia	Valley Forge Military Academy	A Career in Public Accounting
20	Herman C. Heiser, M. S. R. & C. D.	American Management Association, New York	The Internal Auditor & Electronic Data Processing
20	Robert L. Jessee, San Francisco	California Society of C.P.A.s, San Francisco Chapter	New California Code Provisions and Procedural Problems Before the Franchise Tax Board
20	L. C. Moscarello, New York	National Retail Merchants Association, New York	Forum Discussion—Aging of Retail Receivables
20	L. C. Moscarello, New York	N. Y. State Society of C.P.A.s—Metropolitan Controllers Association	Moderator—Application of Electronics to Retail Receivables
21	James P. Colleran, Jr., Cleveland	Cleveland Radio Station KYW Program Sponsored by Ohio Society of C.P.A.s	Panel Member—Personal Federal Income Tax Problems
21	H. O. Reyburn, Tulsa	Texas Society of C.P.A.s, Abilene Chapter	Activities of the American Institute of C.P.A.s
21	Frank P. Smith, New York	Federal Government Accountants Association, N. Y.	The Accountant and His Managerial Future
21	Abner J. Starr, Cincinnati	Textile Group of Cincinnati Association of Credit Men	Financial Operation Ratios for Credit Purposes
21	G. W. Welsch, Dallas	N.A.A., Shreveport Chapter	Current Income Tax Developments
22	Raymond E. Graichen, Philadelphia	Stradley Tax Luncheon, Philadelphia	Buying and Selling a Corporate Business
Feb.			
2	John W. Conrad Chicago	Accounting Seminar—University of Colorado	A Public Accounting Career

Date	*Speaker*	*Organization*	*Topic*
Feb.			
2	Herman C. Heiser M.S.R. & C.D.	Systems & Procedures Association, Cincinnati	Computer at Work
2	Felix Kaufman, M.S.R. & C.D.	Systems & Procedures Association, Cincinnati	Performing Feasibility Studies
2	Michael Shegda, M.S.R. & C.D.	Systems & Procedures Association, Cincinnati	Simulating Production Problems on Computers
8	Norman E. Auerbach, New York	Tax Executives Institute, Inc., New York Chapter	The Problem of Corporate Reorganizations as They Specifically Relate to Goodwill in Corporate Acquisitions
9	Maurice B. T. Davies, Los Angeles	N.A.A., Los Angeles Chapter	Seminar—Communications and Management Control
9	H. O. Reyburn, Tulsa	KOTV Sun Up Program, Sponsored by Oklahoma Society of C.P.A.s	Medical Expenses
9	J. Walker Voris, Los Angeles	N.A.A., Los Angeles Chapter	Discussion Forum—Inventory Management for Profit
10	Henry B. Jordan, Washington	Chief Petty Officer's Mess, Naval Air Station, Anacostia, D. C.	Tax Pointers for the Retired Serviceman
16	Joseph B. Fyffe, Boston	Concord High School, Mass., Weston High School, Mass., Waltham High School, Mass.	Preparing to Become an Accountant
16	Herman C. Heiser, M.S.R. & C.D.	N.A.A., Jacksonville Chapter	Direct Costing
17	Maurice B. T. Davies, Los Angeles	N.A.A., Long Beach	Graphics—A Means of Effective Communication
17	Eldin H. Glanz, Detroit	Michigan Association of C.P.A.s, Metropolitan Detroit Chapter	Panel Discussion—Continuing Tax Considerations
17	Herman C. Heiser, M.S.R. & C.D.	N.A.A., Tampa Chapter	Direct Costing
17	Raymond J. Leisner, Cincinnati	Greater Cincinnati Office Machine Dealers Association	Return on Investment as a Control Aid in Management
17	H. O. Reyburn, Tulsa	American Society of Women Accountants	Problems of Becoming a C.P.A.
17	J. Walker Voris, Los Angeles	Systems & Procedures Association, San Fernando Chapter	A Review of EDP Applications in Business
18	R. K. Batzer, New York	N.A.A., South Florida Chapter	Direct Costing
18	Robert W. Davis, Cincinnati	Institute of Internal Auditors, Cincinnati Chapter	Effective Report Writing
18	William R. Hindman, Louisville	Steel Founders Society of America, Chicago	Costs in the Industry Business Cycle
18	Roy H. Webster, Portland	N.A.A., Newport Chapter	Regulation of Securities Issues by the S.E.C.
22	Joseph E. Tansill, Chicago	Illinois Society of C.P.A.s, Program on Station WLS, Chicago	Discussion—Taxes
23	Donald E. Beattie, Dallas	Texas Society of C.P.A.s, Dallas Chapter	Seminar—Management Reporting
23	Maurice B. T. Davies, Los Angeles	N.A.A., San Fernando Valley Chapter	Selling Accounting to Management
23	William W. Ragsdale, Jr. Birmingham	Shades Valley High School, Birmingham	Accounting as a Career
23 25	Howard L. Swiger, James W. Plate, Rockford	Rockford Chamber of Commerce, Career Nights at Junior High Schools	Careers in Accounting

Date	*Speaker*	*Organization*	*Topic*
Feb.			
24	James E. Gelbert, Pittsburgh	City Farmers Club, Pittsburgh	Farm Tax Problems
25	R. L. Colegrove, New York	Edgemont High School, Scarsdale	Accounting as a Career
25	Tibor Fabian, M.S.R. & C.D.	National Society of Business Budgeting, Dallas	Operations Research in Budgeting
25	Frank H. Gafford, Birmingham	American Society of Women Accountants, Birmingham Chapter	Management Services by C.P.A.s
25	L. E. Hoffman, Tulsa	Society of Petroleum Engineers of the American Institute of Mining Engineers, Tulsa	Income Tax Record Keeping the Easy Way
25	Darwin Ley, Chicago	DePaul University	Tools for the Analysis of the Systems Problem
26	Mark E. Richardson, New York	Controllers Institute, 1960 Southern Conference, Edgewater Park, Miss.	Management Decisions and Taxes
26	Leo V. Tinkham, Chicago	Kentucky Society of C.P.A.s, Louisville	The Defalcation Dilemma
26	Roy H. Webster, Portland	Crown Zellerbach Personnel, Camas, Washington	Personal Income Taxes
Mar.			
1	Tibor Fabian, M.S.R. & C.D.	University of Pennsylvania	Simulation Models in Operations Research
1	James E. Meredith, Jr., Philadelphia	Harvard School of Business Adm.	Management Services by C.P.A.s
2–4	William G. Casey, Boston	A.M.A. Orientation Seminar, New York	Revitalizing the Cost Accounting System
2	Henry B. Jordan, Washington	Rochester T.E.I.	How Federal Income Tax Regulations are Developed
4	Kenneth P. Johnson, Pittsburgh	Career Conference, New Kensington School District	The Profession of Accounting
7	Donald E. Beattie, Dallas	Texas Society of C.P.A.s, Dallas Chapter	Management Reporting
9	Lewis A. G. Martorano, Philadelphia	Rotary Club, Haddonfield, N. J.	Management Services by C.P.A.s
10	Sidney Kess, New York	Accounting Club, City College	Your Future in Tax Accounting
10	Paul D. Yager, Washington	Rotary Club, Bladensburg, Md.	Recent Developments in Federal Income Taxes
14	Jerome Y. Halperin, Detroit	Small Business Management Course sponsored by Wayne State U. and Small Business Administration at Lee Thurston High School	Taxation of Smaller Businesses
17	Robert W. Davis, Cincinnati	N.A.A., Cincinnati Chapter	Federal Taxation
17	James E. Meredith, Jr., Philadelphia	N.A.A., Richmond Chapter	Inventory Management and Production Control
18	William G. Casey, Boston	Harvard Business School	Direct Costing
19	James Neely, Jr., Boston	Ninth Annual Institute for Maine Industry, Colby College	Impact of Data Processing Machines on Business
22	Herman C. Heiser, M.S.R. & C.D.	Illinois Manufacturers Cost Association, Chicago	Direct Costing

Date	*Speaker*	*Organization*	*Topic*
Mar.			
23	Joseph M. Conder, Dallas	Institute of Internal Auditors, Dallas	Cooperation Between Internal Auditor and Independent Public Accountant
24	Raymond J. Leisner, Cincinnati	N.A.A., Cincinnati Chapter	Panel Member—Make or Buy Decisions
24	Harry C. Vournas, Los Angeles	California Society of C.P.A.s, Bakersfield Chapter	Management Services As It Relates to the Small Practitioner
25	Frank H. Gafford, Jr., Birmingham	American Institute of Industrial Engineers, Birmingham Chapter	Panel Discussion—Modern Management Techniques
28	James P. Colleran, Jr. Cleveland	Brooklyn Heights Kiwanis Club	Federal Tax Tips for the Individual
29	Philip L. Defliese, New York	Georgia State Society of C.P.A.s, Atlanta Chapter	Panel Discussion—Current Activities of the Auditing Procedure Committee, A.I.C.P.A.
29	Lewis A. G. Martorano, Philadelphia	Chamber of Commerce of Greater Philadelphia	Product Costing
29	Herman Stuetzer, Jr., Boston	Massachusetts Society of C.P.A.s	Panel Member—Massachusetts State Taxes
30	John J. McCullough, Detroit	Grosse Pointe High School	European Common Market
31	Fred C. Dennis, Cincinnati	Beta Alpha Psi, University of Cincinnati Chapter	Ohio C.P.A. Law
31	James E. Meredith, Jr., Philadelphia	N.A.A., Pittsburgh Chapter	Conference Session Chairman—Operating Budgets

Notes

INTERNATIONAL FIRM

The new address of the Kuala Lumpur (Federation of Malaya) office is as follows:

28–30 Old Market Square
(2nd floor)
Kuala Lumpur, Malaya
Telephones: 83144/6

The address of the Munich, Germany, office has been changed to the following:

Sonnenstrasse 33/v, Aufgang B
Munich 15

The address of the Toronto office has been changed to the following:

100 University Avenue
Toronto 1, Ontario

Mr. Henry Benson, C.B.E., F.C.A., has been appointed by the Minister of Transport as a member of an advisory body of four, with Sir Ivan Stedeford, K.B.E., as chairman, to examine the structure, finance and workings of the organizations at present controlled by the British Transport Commission.

Mr. S. John Pears, on June 1, was elected President of the Chartered Accountants Institute of England and Wales.

BIRMINGHAM

Mr. Bill Goodner has been named a charter member of the recently organized Estate Planning Council of Birmingham.

Mr. Ragsdale served as a member of the Citizens Committee of the Birmingham Chamber of Commerce to study a bond issue proposed by that city.

BOSTON

Mr. Melvin A. Dyson is instructing a course in managerial accounting at Northeastern University.

Mr. J. Paul Finnegan is teaching a course on the Basic Principles of Federal Income Taxation at the Boston Chapter of the American Institute of Banking. He has also been appointed to

the Standing Committee of the United Fund in the Town of Scituate and is Treasurer of the Old Colony Harvard Club for one year.

Mr. Joseph B. Fyffe has been reelected Director of the Harvard Musical Association.

Mr. Higbee is serving as Treasurer and Trustee of the Hingham Public Library; he is also director of the Wompatuck Community Center, Inc.

Mr. Stuetzer recently appeared before the Tax Committee of the Massachusetts Legislature on the sales tax question. He has also recently been elected Chairman of the Board of Selectmen of Hingham.

Mr. William R. Wilson has been elected a member of the Vestry of the Trinity Episcopal Church of Wrentham for two years and is Treasurer for the Salvation Army Unit. He is also serving the town as a member of the Board of Public Welfare and as a member of the Insurance Committee for one year.

CINCINNATI

Mr. Robert W. Davis is serving the United Appeal—Community Chest—Red Cross of the Cincinnati area as Vice Chairman, District Residental Solicitation and Mr. Waterfield is serving as Chairman, General Audit Campaign Committee.

CLEVELAND

The Cleveland Bar Association presented an award to the Firm in acknowledgment of the meritorious contribution of time, effort and skill in behalf of the Association in directing and certifying the audit of ballots cast in the Judicial Campaigns conducted by the Association for the past 25 years. The citation is reproduced on page 52 of this issue.

DALLAS

Mr. Arthur is Chairman of the Dallas Chapter of the Texas Society of C.P.A.s' Committee on Investigating Use of Cooperative Students from Dallas Area Universities. Mr. Joseph M. Conder is serving as a member of this Committee.

Mr. Welsch is Chairman of the Grounds & Scoreboard Committee of the Golf Executives, Inc. and is also Co-Chairman of the Communications Committee.

DETROIT

Miss Geraldine Dominiak and Mr. Lawrence Doyle were recently elected to membership in the Catholic Accountants' Guild.

Mr. Gofrank is President for 1960 of the World's First Kiwanis.

Mr. Lyons is serving as President of the United States Men's Curling Club; he is also President of the Paul Bunyon Club.

Mr. Teetzel is a member of the Board of Directors of the Lochmoor Club, Grosse Pointe.

The following staff members have beene elected to membership in the Detroit Chapter of the N.A.A.:

Alan E. Beatty	Ronald Hamburger
Morley P. Carscallen	Vincent J. Lico
Norman N. Griffin	David Mandell

Elwin C. Meyers

HARTFORD

Mr. Berthoud is serving as Treasurer of the University of Pennsylvania's Alumni Club of Greater Hartford.

LOS ANGELES

Mr. Bowles is serving as a member of the California State Board of Accountancy C.P.A. Complaints Committee for 1960.

Mr. Charles R. Cook is Treasurer of the Nela Shrine Club and is also New-Club Chairman of the Optimist Club of Los Angeles.

On May 20, at a dinner attended by the Los Angeles partners and his fellow associates, Mr. Alfred F. Matt was honored on his impending retirement. As a token of the high esteem in which he is regarded by his many friends, he was presented with a set of golf irons and with a plaque.

Miss Madonna E. Newburg has been admitted to membership in the A.I.C.P.A.

Mr. James M. Nicolai is serving as a member of the Board of Directors for 1960 of the Los Angeles Junior Chamber of Commerce.

Mr. Warner is a member of the Finance Committee of the California Club, Treasurer of the Nixon for President Committee for California and Treasurer of the Los Angeles Citizens Committee for School Development.

The following members of the Los Angeles staff have received C.P.A. certificates:

Manuel J. Armendariz	Carl M. Moser
John E. Cutler	Edward R. Pasini
Neal M. Edwards	Gerald R. Perlstein
Edward L. Lengtat	Robert A. Poons

The First Annual Staff Golf and Bridge Outing was held at the Riviera Country Club on April 25 and was declared by those in attendance as an outstanding success. In addition to the golf and bridge tournaments, other games and activities were indulged in by those present.

A perpetual golf trophy was graciously donated to the office by Coopers and Lybrand, Mexico City. Sr. Rolando Ortega, a representative of that office, temporarily assigned to Los Angeles, presented the trophy to Mr. Warner, who was gross winner by a considerable margin.

LOUISVILLE

Mr. Thomas K. Baer is Vice President for 1960–61 of the Junior Chamber of Commerce.

Mr. Glore is again participating in the Heart Fund Drive for the city of Louisville.

Mr. Norris E. Krall has been awarded his C.P.A. certificate.

NEW YORK

Mr. Auerbach is serving as a member of the Estate Planning Council of New York City.

Mr. Bardes is serving as a member of the Committee on Taxation of the National Association of Manufacturers. He is also Chairman of the Public Accounting Division of the Boy Scout Capital Camp Campaign.

Mr. Doty has been elected to the Board of Governors of Arthritis and Rheumatism Foundation, Inc.

Mr. Fernald received an honorary LL.D. on February 14 at the 125th Anniversary of Marietta College, Marietta, Ohio.

The following members of the New York staff have successfully completed the November, 1959 examination:

J William Biggs	George J. Lamoureux
Donald L. Carlile	James J. Quinn
Robert M. Fischer	Julius L. Ross
Frederick D. Heiman	Albert W. Russ
Daniel J. Klein	Arthur L. Simon

John H. Winters

PHILADELPHIA

Mr. Edward F. Habermehl has been appointed auditor of Warrington Township, Bucks County.

Mr. Moneta has been elected Treasurer of the Philadelphia Country Club. He has also been appointed to the Board of Governors of Commerce and Industry Council of the Greater Philadelphia Chamber of Commerce.

Mr. Kenneth J. Mutzel is a member of the Borough Council of Barrington, Camden County, N. J.

Mr. Schweitzer is serving as Chairman of the Audit & Report Committee of the 1961 Campaign of the United Fund Torch Drive of Greater Philadelphia Area.

PITTSBURGH

Mr. Gelbert is Chairman of the Planning Committee of the Pennsylvania State University Fourteenth Annual Tax Seminar.

Mr. Kenneth P. Johnson has been elected Treasurer of Northern St. Clair Home Owners Association.

Mr. Kulzer has accepted an invitation to serve on the Community Advisory Committee of the Junior League of Pittsburgh, Inc.

PORTLAND

Mr. Roy H. Webster is a member of the Recreational and Natural Resources Committee of the Chamber of Commerce for the year 1960. He is also Treasurer and a member of the Board of Trustees of the Portland Civic Theatre.

ROCKFORD

Mr. John S. Eaton was a delegate to the inauguration of the new President of Rockford College.

SAINT LOUIS

Mr. John D. Mains appeared as a judge on an educational television program sponsored by the Internal Revenue Service; he has also been elected a member of the Board of Education of his local school district in Belleville, Illinois.

SAN FRANCISCO

Mr. Giles has been reappointed Consulting Professor of Public

Accounting at Stanford University Graduate School of Business for the Academic Year 1960–61.

Mr. Carl F. Grove is serving as Chairman of the California Society of C.P.A.s subcommittee appointed to plan and present a technical session entitled "Mechanizing the C.P.A.'s Own Office" at the Annual Meeting in 1960.

Mr. Huss is serving as a member of the House Committee of the St. Francis Yacht Club and is also a member of the Tax Section of the San Francisco Chamber of Commerce.

Mr. Joseph J. Hyde has been admitted to membership in the A.I.C.P.A.

Mr. Donald G. Perry recently served as an instructor in staff training programs for accountants at the University of California, Santa Barbara.

Mr. Schroeder is a member of the Finance Committee of the Palo Alto Hills Golf and Country Club.

SEATTLE

Mr. Aiken is a member of the Board of Trustees for 1960 of the Plymouth Congregational Church, Chairman of the Budget Committee of the Tulsa Community Chest for the coming year and has been elected to the Advisory Committee for Tulsa University's Accounting Conference.

Mr. Bernhard U. Krummel has been elected to the Board of Trustees of the German Old Peoples Home Association of Seattle and has been reappointed a member of the Finance and Management Committee of the Board of Trustees of Group Health Cooperative of Puget Sound.

TULSA

Mr. McKibben is serving as Treasurer and a member of the Board of Directors of the Tulsa Y.M.C.A. for 1960–61.

Mr. Reyburn is Treasurer of the First Baptist Church and has been appointed a Trustee and Endowment Counselor of the Tulsa Psychiatric Foundation, Inc.

Messrs. Don H. Freeman and Jack A. Sharp, Jr. have been admitted to membership in the Oklahoma Society of C.P.A.s.

WASHINGTON

Mr. Yager participated in the April meeting of the American Institute's subcommittee on Administration, Procedure and Miscellaneous Taxes in Raleigh, North Carolina.

Lybrand, Ross Bros. & Montgomery

Offices

Cities	*Addresses*
BALTIMORE 2	First National Bank Building
BIRMINGHAM 3	First National Building
BOSTON 10	80 Federal Street
CHICAGO 4	Board of Trade Building
CINCINNATI 2	Carew Tower
CLEVELAND 14	Union Commerce Building
DALLAS 2	First National Bank Building
DETROIT 26	Book Building
HARTFORD 3	37 Lewis Street
HOUSTON 2	1114 Texas Avenue
LOS ANGELES 13	510 South Spring Street
LOUISVILLE 2	Heyburn Building
NEW YORK 4	Two Broadway
PHILADELPHIA 2	Packard Building
PITTSBURGH 22	Oliver Building
PORTLAND 4	Executive Building
ROCKFORD	119 North Church Street
SAINT LOUIS 1	411 North Seventh Street
SAN FRANCISCO 4	100 Bush Street
SEATTLE 1	Skinner Building
TULSA 3	Philtower Building
WASHINGTON 5	Investment Building

Lybrand, Ross Bros. & Montgomery

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Robert L. Aiken	Seattle
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J. K. S. Arthur	Dallas
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Philip Bardes	New York
R. Kirk Batzer	New York
Hermon F. Bell	New York
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Norman A. Bolz	Detroit
Joseph W. Bower	Pittsburgh
Herbert G. Bowles	Los Angeles
Louie M. Bradley	Los Angeles
Roger F. Burd	Philadelphia
J. Edward Burke	New York
Hilton R. Campbell	New York
Edward G. Carson	New York
Harold C. Chinlund	Baltimore
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Reed L. Colegrove	New York
James P. Colleran	Cleveland
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John J. Fox	Detroit
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Christopher H. Knoll	New York
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Harry W. Moore	Los Angeles
Louis C. Moscarello	New York
Edward P. Mullen	Philadelphia
Flay L. Murphy	Chicago
Robert W. Myers	Rockford
Edwin P. Noell	Cleveland
John C. Padgett	Cleveland
Charles A. Pearson	Los Angeles
Glenn O. Petty	Philadelphia
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